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PENSIONS & July 24, 198

InvestmentAge

The newspaper of corporate and institutional investing $6 an issue - $110 a year

Bill hikes labor pension role

By Joel Chernoff

WASHINGTON — Corporations would be required to give labor an equal say in the investment and administration of all retirement plans under a bill passed by the House Education and Labor Committee.

Business experts say the requirement threatens the existence of the private retirement system.

The provision was the nasty surprise in a mixed bag of amendments passed by various House and Senate committees in the past two weeks as part of efforts to draft a $5.3 billion budget reconciliation bill. In some cases, provisions dealing with the funding of post-retirement health care benefits and surplus asset reversions carried so many restrictions as to make them unworkable.

The amendment requiring joint administration, sponsored by Rep. Peter J. Visclosky, D-Ind., would require single-employer defined benefit and defined contribution plans to have jointly trusteed boards, similar to those existing for multiemployer pension plans. The bill would extend beyond organized labor to include non-union employees.

The amendment was attached to the House Education and Labor Committee's budget-reconciliation bill that was voted out of committee July 13, and thus is assured serious consideration by Congress.

Business groups said such a requirement would be devastating for the future of defined benefit plans in particular. They said many employers — required to assume the entire investment risk — would rather end their plans than share investment and other responsibilities with employees.

The Visclosky amendment "puts defined benefit plans into a death spiral," said Howard Weizmann, executive director of the Association of Private Pension and Welfare Plans, Washington.

"Employers have been pushed to the edge by government regulation. This could push them over," said Henry Savath, principal at A. Foster

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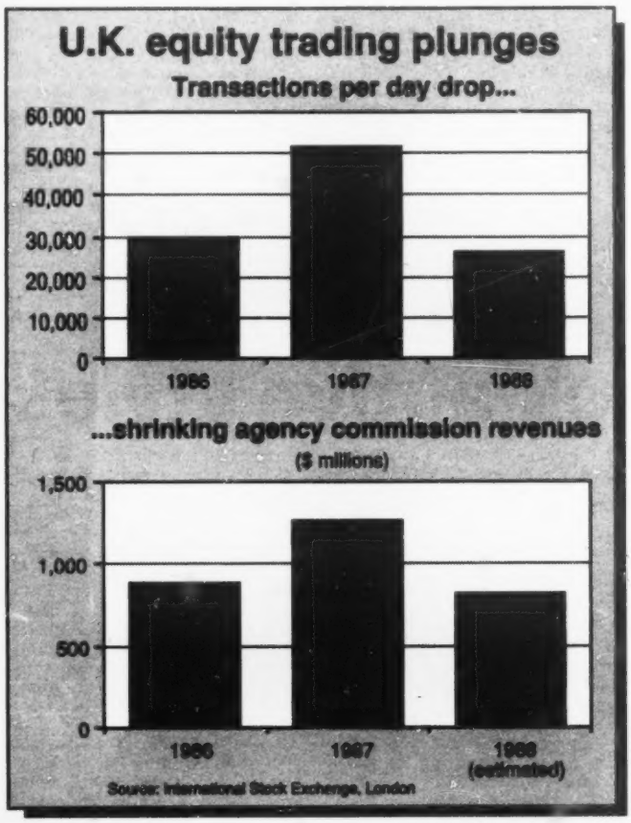

British reluctant

Directed commissions snubbed

By Joel Chernoff

LONDON — "Soft commissions" are running into the hard wall of reality in Great Britain.

A now powerful factor in the U.S. stock market, where more than 20% of U.S. institutional trades go toward generation of soft-dollar rebates, the trend has skipped across "the pond" into the International Stock Exchange in London.

Some don't like it one bit. In fact, Britain's Securities and

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Paying for approval

Ramada offer is bittersweet

By Marlene Givant Star

PHOENIX, Ariz. — Ramada Inc. is offering shareholders a generous cash payment in exchange for approval of a strategic corporate restructuring proposal and anti-takeover provisions that give insiders and a new ESOP more than 20% of the company through stock and options.

But the up to $7-a-share spoonful of sugar being offered won't help the medicine go down, according to Institutional Shareholder Services Inc., Washington, and many institutional investors. Charging the bundled items, which include a controversial "stakeholder charter provision," will only serve to impair the long-term value of the company, ISS registered an objection to the proposal with the Securities and Exchange Commission July 19 and is urging its clients to do the same.

Shareholders will vote on the proposal, which downsizes Ramada to a purely gaming company, at the July 31 annual meeting.

Management's stockholdings, options and restricted shares and the ESOP holdings would total more than 20% of the ownership of the company under the proposal. Along with supermajority requirements for mergers and 80% charter and bylaw lock-ins under the proposal, "this company would not only be protected, it would be sealed up tight," according to an ISS proxy analysis by Ian W. Macoy, senior analyst.

In addition, the proposal includes a stakeholder charter provision. These controversial measures, which are becoming more popular, say corporations should consider not only their shareholders' interests but also those of suppliers, communities, employees and others.

Ramada's provision does not clearly state shareholder interests take precedence over those of other parties, and ISS fears the board could refuse a takeover offer that is good for shareholders on the grounds that, for instance, local jobs might be lost.

Also, the stakeholder charter provision does not specify the relative weight the board of the restructured company, to be called Aztar Corp., would give to various factors in considering a tender offer or merger.

ISS also believes dilution associated with additional stock awards to key employees and the 1989 stock and incentive plan are excessive.

Bundled proposals like Ramada's could become much more common. "We have seen (them) before at INCO, Morton-Thiokol and other companies, and have no doubt

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Ramada wants to shed its hotel operations and become a pure gaming company. In exchange for their approval of the proposal, shareholders would get up to $7 per share in cash.

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LATE NEWS

California fund buys mall stake

CHICAGO — The California Public Employees Retirement System is expected to pay more than $200 million for a 50% stake in a suburban Chicago shopping mall.

The $54 billion California fund's investment board approved the purchase recently. Its adviser, TCW Realty Advisors, Los Angeles, is negotiating a final price with Homart Development Co., the real estate development arm of Sears, Roebuck and Co. and owner of the 50% share.

The remaining 50% interest in the shopping center, the 2.3 million-square-foot Woodfield Mall, Schaumburg, is owned by Taubman Realty Group of Detroit.

Participant-loan ruling attacked

WASHINGTON — The Department of Labor said pension plans must charge the prevailing rate used on similar commercial loans when lending money to plan participants.

The department made a key concession, however, in making the regulation effective 90 days after its July 20 publication date. It had proposed making the rule retroactive to Jan. 1, 1975.

Organized labor blasted the decision. The rule "is an unwarranted restriction on the investment decisions of employee benefit plans and will effectively prevent them from serving as a source of mortgage loans at times when the commercial sector abandons the mortgage market . . .," Robert A. Georgine, chairman of the National Coordinating Committee for Multiemployer Plans, Washington, said in a statement.

Manager pushes recapitalization

GREENWICH, Conn. — A money management firm and major institutional stockholder of LIN Broadcasting Co., New York, is taking an unusual lead role in suggesting LIN management opt for a recapitalization — and said it has even lined up the financing — rather than accept a hostile takeover bid by McCaw Cellular Communications Inc.

Frederick Moran, president of Moran Asset Management, Greenwich, Conn., late last week wrote Donald Pels, president and chairman of LIN, and suggested a detailed recap plan. Under the plan, LIN would borrow funds to finance the recap and then pay shareholders a cash dividend of $96 per share.

Mr. Moran, whose firm owns about 500,000 shares of LIN, maintains even if McCaw Cellular, in Kirkland, Wash., pays the $127.50 per share price, LIN shareholders would significantly receive less than full value for the company.

GE partnership does realty deal

STAMFORD, Conn. — GE Investments, moving to make its mark quickly as a manager of outside assets, bought a stake in a San Diego property as the first investment for its $350 million equity real estate limited partnership.

GE Investment Realty Partners I invested $26 million for just under a 50% interest in the Naiman Tech Center, a 650,000-square-foot research and development park and office complex. The other half is owned by Naiman Co., San Diego, which developed the property.

Geoffrey Norman, executive vice president of GE Investments, said a major life insurance company he declined to identify provided $70 million in debt. The partnership will hold a first mortgage on the property.

The partnership's investors include the pension funds of General Electric Co., BATUS Inc., Champion International Corp., Combustion Engineering Inc., Eli Lilly & Co., Ford Motor Co., Unisys Corp., Perkin-Elmer Corp. and General Dynamics Corp.

ITT increases allocation to GICs

NEW YORK — ITT Corp.'s savings plan has allocated an additional $126 million to Bankers Trust Co. to be invested in guaranteed investment contracts, according to Eileen Leahy, manager of pension fund trusts. The amount is in addition to $310 million of GICs Bankers already manages for ITT's savings plan. Ms. Leahy declined to disclose further information.

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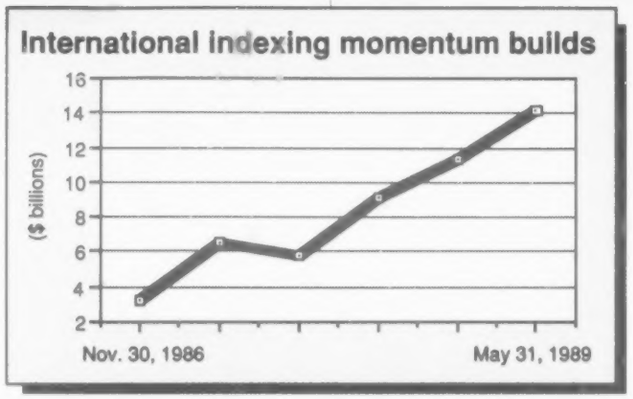
Questionnaire deadline nears

The deadline is nearing for inclusion in *Pensions & Investment Age*'s annual survey of master trust, master custodial and global custodial banks. In order to be included in the Sept. 4 issue, questionnaires must be returned by Aug. 1. Also, questionnaires will be sent out shortly for *P&I Age*'s annual real estate manager profiles. The questionnaire deadline for that directory, which will be published Oct. 2, is Aug. 28. If you have any questions, please call Christine Philip at (312) 649-5217.



Indexing lags domestically

Domestic index funds shrank on a market-adjusted basis for the first time since *Pensions & Investment Age* began tracking their asset growth.

Domestic equity funds grew $12.26 billion between Nov. 30 and May 31 — to $137.68 billion. But that 9.8% increase became a 6.3% decrease when adjusted to reflect the Standard & Poor's 500 Stock Index rise of 17.11%.

Similarly, domestic fixed-income funds grew $2.41 billion since Nov. 30, to $49.51 billion — an increase of 5.1% — but shrank 0.6% on a market-adjusted basis. For the six months ended May 31, the Shearson Lehman Hutton Government/Corporate Bond Index rose 5.78%.

Only international equity index funds showed market-adjusted growth, climbing $3.32 billion to $13.97 billion. When adjusted for the decline in the Morgan Stanley Capital International Europe Australia Far East Index, the growth of 31% jumps to 37.1%. (Of the $14.14 billion in international indexing, only $173 million is in fixed income.) The EAFE, expressed in U.S. dollar terms with no dividends reinvested, dropped 4.3% during the period.

The numbers above exclude ANB Investment Management Co., which would not provide a May 31 breakout.

Overall, externally managed index funds grew about 8.7%, or $16.92 billion, during the period, to $210.72 billion, according to the semiannual *P&I Age* survey of index fund managers.

The decline in domestic index funds seems to reflect a desire on the part of pension executives to jump into the bull market on Wall Street.

For example, Putnam Cos. Inc.,

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College on new course

By Christine Philip

COLUMBUS, Ohio — The $282 million Ohio State University endowment, Columbus, has allocated $65 million to a core of index funds, including its first steps into small-capitalization stocks and international investing.

The moves followed a strategic asset allocation study, conducted by Ennis, Knupp & Associates, Chicago. No consultant was used in the search process.

According to Stephen F. Messerly, assistant treasurer, three index managers were hired: Wells Fargo Investment Advisors, San Francisco, to run $30 million in a Standard & Poor's 500 Stock Index fund and $10 million in an international index fund matched to the Morgan Stanley Capital International Europe Australia Far East Index; R. Meeder & Associates, Dublin, Ohio, to run $15 million in a small-cap index fund, matched to the smallest 100 of the S&P 500 index; and W.R. Lazard, New York, to handle $10 million in a broad domestic fixed-income index fund, matched to the Shearson Lehman Hutton Government/Corporate Bond Index.

Assets for the new hires came from reductions in the accounts of two equity managers — The Chicago Corp., Chicago, and Siebel Capital Management, Larkspur, Calif.; the liquidation of a mutual fund managed by Neuberger and Berman, New York; and from internally managed assets.

The fund is in the process of finalizing contracts with each of the three managers selected. ■

Funds seek active styles

By Trudy Ring

Big moves by big funds dominated money management changes in the second quarter, and active strategies again outdrew passive ones to continue the pattern of the past several quarters.

The $1.36 billion in active fixed-income hirings reported in *Pensions & Investment Age* during the quarter included three allocations of $300 million. The $1.26 billion in active equity hirings reported included six allocations of $100 million or more.

There were no hirings reported for bond index fund management, and the only hiring reported for stock index fund management was for an undisclosed amount. Structured and quantitative strategies, however, were popular for both bonds and stocks.

The numbers are based only on moves reported in *P&I Age* during the quarter; there might have been other moves that were not publicized.

One of the $300 million bond hirings was of Goldman, Sachs Asset Management, New York, by the $10.4 billion American Information Technologies Corp. pension fund, Chicago. The portfolio will be duration-matched.

There also were two hirings for $300 million each by the $2.7 billion Wyoming Permanent Fund. The two managers selected, Criterion Investment Management Co., Houston, and Duff & Phelps Investment Management Co., Chicago, are the fund's first outside managers.

Criterion also had two other hirings reported during the quarter, for a total of $370 million in new business.

Besides the Goldman hiring, the popularity of structured strategies was indicated by Consistent Asset Management Co.'s two hirings for a total of $67 million. The firm, based in Wilmington, Del., describes itself as quantitative.

The equity area was fueled by two public funds. The $3.1 billion Kansas Public Employees Retirement System hired Delaware Investment Advisers, Philadelphia, to manage $280 million, and Loomis, Sayles & Co. Inc., Pasadena, Calif., to run $150 million.

In addition, the $13.1 billion Minnesota State Board of Investment hired four managers for $100 million each — Concord Capital Management, San Mateo, Calif.; Franklin Portfolio Associates Trust, Boston; Rosenberg Institutional Equity Management, Orinda, Calif.; and Sasco Capital Inc., Fairfield, Conn. The board drew the money from a $2.5 billion stock index fund. Both Franklin Portfolio Associates and Rosenberg Institutional Equity describe themselves as quantitative managers.

Consultants said they have been doing more searches for active rather than passive management recently. Ann Wohler, senior vice

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Most new accounts* 2nd quarter 1989

Firm	New accounts
Bankers Trust	4
Fisher Investments	4
Sanford C. Bernstein	3
The Chicago Corp.	3
Criterion Investment	3
Morgan Stanley/Chicago	3
NCM Capital Mgmt.	3

* As reported in *Pensions & Investment Age*

Most new assets* 2nd quarter 1989

Firm	$ millions
Criterion Investment	370
Duff & Phelps	300
Goldman, Sachs	300
Delaware Investment	280
Loomis, Sayles	165
Sanford C. Bernstein	140

* As reported in *Pensions & Investment Age*

Whirlwind surrounds stock plans

$19 billion financed in '89 despite debate over value

By Barry B. Burr

U.S. corporations have financed more than $19.2 billion worth of employee stock ownership plans so far in 1989, dwarfing the estimated $5.6 billion in ESOPs set up for all of 1988.

ESOP financings announced by 80 major corporations total at least $17.733 billion to date, and an estimated 250 smaller companies have established ESOPS valued at less than $10 million each, or an estimated $1.5 billion in aggregate.

Yet, academics and other analysts contend corporate America's rush to start or greatly expand ESOPs is based on their anti-takeover appeal or on a costly misunderstanding of the potential tax and economic advantages.

An investment banker, who heads up a Wall Street firm's ESOP financing area, agreed with some of their economic arguments, that unleveraged ESOPs may offer more cost advantages than leveraged ESOPs, though in the entire context of employee benefits he still believes leveraged ESOPs are better.

The number of new or expanded ESOPs this year could be higher than the figures show because there are no public corporate reporting requirements for the plans. The data came mainly from the National Center for Employee Ownership, Oakland, Calif., a private group that tracks announcements of ESOPs.

Until Congress began talking seriously about reducing the tax advantages of ESOPs, the trend showed no sign of abating. Since July 10 — the date the House Ways and Means Committee chose as the effective date of a proposal to restrict tax breaks — ESOP financings have slowed significantly, corporate and Wall Street executives said. ESOPs are "on hold," said Paul J. Mazzilli, principal, Morgan Stanley & Co., New York.

GTE Corp., Stamford, Conn., specifically set up a $700 million ESOP, including issuing private-placement debt, on July 10 to meet the new effective date, according to Thomas Mattausch, director-public relations services for GTE.

GTE set up the ESOP solely to obtain the tax benefits to reduce the cost of providing an existing corporate matching payment, heretofore made in the form of stock paid from corporate operating cash, he said. Employees will see no change in benefits, Mr. Mattausch said.

GTE issued 12 million shares to the ESOP from those already in the treasury. Mr. Mattausch said the company will repurchase the shares on the open market, plus another 11 million shares that remain to be bought back in a share repurchase program announced last August.

Among other more recent ESOPs are: $785 million worth of shares at Xerox Corp., Stamford, Conn.; $500 million at Delta Air Lines Inc., Atlanta; $270 million at Armstrong World Industries Inc., Lancaster, Pa.; $190 million at Levi Strauss & Co., San Francisco; $150 million at General RE Insurance Corp., Stamford, Conn.; $100 million at Citizens & Southern Corp., Atlanta; and $100 million at Burlington Industries Inc., Greensboro, N.C. Both Levi Strauss & Co. and Burlington Industries coincidently had been taken private in recent years in leveraged buy-outs.

Meanwhile, Moody's Investors Service Inc., New York, downgraded Colgate-Palmolive Co.'s debt rating, the first attributed to the creation of a leveraged ESOP.

25 largest ESOP financings of 1989

	$ millions
Bell Atlantic	1,000
BellSouth	1,000
Procter & Gamble	1,000
Xerox	785
ITT	700
GTE	700
Ameritech	700
HCA Psychiatric	600
3M	550
Whitman	500
U S WEST	500
Lockheed	500
Southwestern Bell	500
Anheuser-Busch	500
Delta	500
May	400
Colgate-Palmolive	400
Melville	357
Sara Lee	350
Tribune	350
FMC	300
Upjohn	300
Boise Cascade	300
Armstrong World Industries	270
Unisys	250

Source: National Center for Employee Ownership, Oakland, Calif.; and others

The lower debt rating could translate into overall higher financing costs for the New York-based company and diminish the borrowing-cost advantage the formation of its $410 million ESOP would provide, if investors agree with the new credit assessment, said Dory Gaforek, associate director at Moody's.

The new analyses that question the economic and other benefits of ESOPs could, if accepted, have a profound effect in slowing formation of the plans. Mark A. Wolfson, the Joseph McDonald Professor at Stanford University's Graduate School of Business, concludes the plans aren't neces-

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Congress to decide future of public-company ESOPs

By Joel Chernoff

WASHINGTON — Employee stock ownership plans for public corporations are down but not out on Capitol Hill.

Nearly two weeks ago, the House Ways and Means Committee dealt the plans a crushing blow by voting to repeal the deductibility of dividends for most ESOPs. But the Senate Finance Committee, where the next round will take place — possibly as soon as this week — is viewed as more favorable to the plans.

Early signals suggest the Senate might retain dividend deductibility, but reject generous transition rules contained in the House bill.

Meanwhile, activity in creating new ESOPs has slowed since July 10, as employers wait to see what action finally is taken.

"I don't think people will stampede into doing ESOPs until the tax questions are clear," said Marvin H. Greene, vice president at TPF&C, New York.

The battle lines are forming over which restrictions eventually will be imposed on ESOPs. Arguments reflect whose ox will be gored: whether benefits for privately held firms will be preserved over those for publicly held corporations, or whether a select group of companies stands to benefit from transition rules while the door is shut on some future transactions.

The outcome will have a dramatic effect on companies that have not yet instituted ESOPs following Polaroid Corp.'s successful use of an ESOP in fighting a hostile takeover bid by Shamrock Holdings Inc. earlier this year.

The ESOP provisions are attached to budget-reconciliation legislation designed to raise $5.3 billion during fiscal 1990, which starts Oct. 1. ESOP rules make a major contribution to the revenue-raising effort: The ESOP provisions are designed to raise some $1.7 billion next year and a total of $13.2 billion between 1990 and 1994.

At this point, ESOP advocates concede the loss of the 50% exclusion from taxes on interest paid to qualified lenders such as banks, insurance companies and mutual funds. Also, no one expects Congress to back down from reversing an Internal Revenue Service position that permitted the sale of ESOP debt on the public market.

But those provisions — whose repeal was proposed June 6 by Rep. Dan Rostenkowski, D-Ill., chairman of the House tax-writing panel — are more important to private companies financing ESOPs than to publicly held ones.

The financial linchpin for public-company ESOPs comes from the deductibility of dividends provision. Public companies typically contribute convertible preferred shares yielding a high coupon to their ESOPs. The coupon is used to pay down the ESOP debt, and can be set roughly at the level of interest payments on the ESOP loan. The company deducts the value of the dividend, which it could not do for its regular stock shares.

In contrast, much of the value of the interest-exclusion has been gained by the lender, and typically results in only a 15% — or 1.5 percentage points based on a 10% loan rate — decrease in the interest rate on a loan.

Congress believes tax benefits are not being adequately passed through to ESOP participants. In introducing his bill, S. 1303, Senate Finance Committee Chairman Lloyd Bentsen, D-Texas, said the partial-interest exclusion "is being used in a manner that re-

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RJR fund's trades show patience might not pay

By Joel Chernoff

NEW YORK — An analysis of trades done for the RJR Nabisco Inc. pension fund raises questions on the value of "patient trading," and criticizes a widely used method of measuring trading costs.

The Kidder, Peabody & Co., New York, study casts serious doubts on how much money institutional investors can save by waiting days or even weeks to strike trades at desired prices.

It also criticizes a trading-cost measurement tool offered by Abel/Noser Corp., New York.

In its analysis of the establishment of a small-capitalization portfolio for the RJR Nabisco pension fund, Kidder found patient trading cost the fund 213 basis points a share, while Abel/Noser's methodology showed the fund made a profit of 28 basis points a share.

"The harsh reality is that poor measurements of trading costs can be dangerously misleading," wrote authors Stephen G. Bodurtha, a vice president at Kidder and Thomas E. Quinn, principal of Cornerstone Capital, Atlanta, and formerly chief investment officer for RJR Investment Management Inc.

Last year, RJR's $2.5 billion pension fund, together with Kidder, decided to measure the costs of constructing a $40 million small-capitalization stock portfolio through patient trading. They compared the costs of trading using Kidder's cost measurement system with the systems offered by Abel/Noser and SEI Corp.

What's different about the trading-cost measurement system — the implementation shortfall system — applied in the Kidder study is its attempt to measure the opportunity cost of not being able to complete trades at a given time — which the other two systems ignore.

"I think it's great," said Eric Fisher, vice president at the $34 billion College Retirement Equities Fund, New York. "I think this is really the right way to do it, by measuring missed opportunities."

The Kidder study "really points out the inadequacy of how we are measuring trading," said Wayne Wagner, partner at The Plexus Group, Santa Monica, Calif.

Mark Edwards, manager-internal equities for the $12 billion Minnesota State Board of Investment, St. Paul, has been using the implementation shortfall methodology for about two years. "Unfortunately, very few people understand it, including the traders," he said.

The study came from a test of whether patient trading can save money for large institutional investors.

In recent years, some large pension funds — such as CREF, the $50 billion California Public Employees' Retirement System, the $2.3 billion Deere & Co. pension fund and the $3.6 billion General Dynamics Corp. pension fund — and money managers have attempted to get paid for providing liquidity to the market, especially when their trades are driven by price, rather than by time-sensitive information.

In providing liquidity, investors have used a variety of techniques. Some place limit orders to buy or sell a set amount of stock at a particular price. Others disclose their interest in a stock but don't say whether they want to buy or sell and in what quantity. Some ask others to reveal their trading interests first, and then select which trades to execute.

The illiquidity of the stocks involved — a 250-stock portfolio designed to track the Russell 2000 index — made purchase of the entire portfolio in one day "imprudent," according to the study. The average bid-ask spread was 2.64% for the stocks, and the proposed trade size averaged 227.18% of the average daily trading volume.

Kidder estimated the cost of a conventional trading program would be at least 200 basis points and easily as high as 350 basis points.

To trim those costs, the authors devised an alternative trading strategy: Each day, they identified a group of stocks from the 250 that were underperforming the Russell 2000 index from the previous night's close. They then submitted limit orders to buy the underperformers; at night, they submitted the remaining buy list to an electronic crossing network.

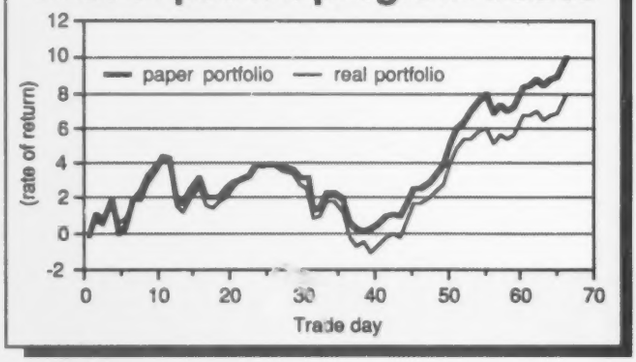
RJR only purchased stocks at its terms, which in the early days were set equal to the prevailing bid price for each stock. After 75% of the portfolio was purchased, the fund started bidding more aggressively, which the study found added 40 basis points to its costs.

For the 67-day buying period, RJR ended up paying an average of 1 cent per share less than the midpoint of the bid-ask spread prevailing at the time the limit orders were submitted.

But traditional methods of measuring the success of the program were misleading because they failed to measure the oppor-

Continued on page 41

Cost of patient program trades



P&I Age Corporate Top 100

Company	ABO	PBO	Plan assets	Plan assets in excess of PBO	Actual return on plan assets*	Net periodic pension expense (income)	Pension expense as a % of adjusted net income	Plan assets as a % of corporate assets	ABO as a % of shareholders equity
Aetna	905.5	1,378.0	1,551.0	173.0	124.4	3.6	0.5	1.9	13.9
Alcoa OP	2,466.5	2,595.2	2,557.1	-38.1	228.0	68.3	7.3	24.3	53.2
Alcoa UP	19.2	21.1	0.2	-20.9	-	-	-	-	-
Allied-Signal OP	2,794.0	3,163.0	3,571.0	408.0	565.0	61.0	11.6	35.7	85.5
Allied-Signal UP	602.0	615.0	570.0	-45.0	-	-	-	-	-
American Brands OP	565.6	713.9	934.1	220.1	11.3	19.6	3.3	7.7	22.7
American Brands UP	389.1	426.5	369.0	-57.5	-	-	-	-	-
American Cyanamid	982.5	1,109.8	1,096.7	13.1	115.4	30.0	8.9	23.9	47.6
American Electric	720.2	902.2	1,075.7	173.5	129.2	(0.7)	NM	7.5	17.0
Ameritech	5,496.3	7,194.7	10,766.1	3,571.4	1,273.1	54.2	4.2	56.2	82.4
Amoco	1,692.0	2,049.0	2,500.0	451.0	304.0	7.0	0.3	8.4	12.7
AMR	1,611.0	1,938.4	1,701.5	-236.9	-210.5	62.1	11.5	17.5	48.8
Armco	1,761.0	1,913.4	1,589.0	-324.4	-175.4	66.6	31.4	57.0	197.8
Atlantic Richfield OP	1,243.0	1,392.0	2,152.0	760.0	180.0	(6.0)	NM	10.0	19.9
Atlantic Richfield UP	172.0	178.0	-	-178.0	-	-	-	-	-
AT&T	16,972.0	18,157.0	28,462.0	10,305.0	3,363.0	(363.0)	NM	81.0	148.0
Batus OP	810.3	1,043.8	1,277.7	233.8	131.9	12.5	2.3	11.1	35.9
Batus UP	49.0	58.3	17.1	-41.2	-	-	-	-	-
Bell Atlantic	7,018.6	8,197.1	9,669.5	1,472.0	1,191.3	165.8	11.2	39.1	76.5
BellSouth	6,800.2	8,319.6	9,136.9	817.3	1,110.8	137.2	7.6	32.1	57.4
Bethlehem Steel	3,833.2	3,968.7	1,628.6	-1,156.8	270.4	185.8	31.6	36.6	214.0
Boeing	4,310.0	5,246.0	5,638.0	392.0	454.0	173.0	22.0	44.7	79.8
Caterpillar OP	1,677.0	2,001.0	2,502.0	501.0	582.0	6.0	1.0	60.8	40.8
Caterpillar UP	1,504.0	1,517.0	1,335.0	-182.0	-	-	-	-	-
Champion International	848.7	944.6	965.0	20.0	109.7	16.6	3.5	14.4	2.5
Chevron OP	2,588.0	2,963.0	3,756.0	793.0	395.0	74.0	4.0	11.1	17.5
Chevron UP	103.0	113.0	1.0	-112.0	-	-	-	-	-
Chrysler	7,328.3	7,405.9	4,358.3	-3,047.6	363.2	585.3	35.8	9.0	96.7
CIGNA	714.9	1,018.9	1,047.2	28.3	93.9	30.0	6.0	1.9	13.6
Commonwealth Edison	1,357.0	1,676.0	1,879.0	203.0	200.0	12.0	1.6	10.5	17.1
Consolidated Edison	1,958.0	2,508.0	2,577.0	69.0	285.4	56.0	8.5	27.0	40.4
Deere OP	924.0	1,192.0	1,284.0	92.0	8.0	18.0	5.4	24.5	37.6
Deere UP	1,022.0	1,077.0	899.0	-178.0	-	-	-	-	-
Delta Air Lines	2,117.5	3,065.4	2,704.7	-360.6	18.1	120.9	28.3	47.1	95.9
Digital	448.9	1,375.9	1,592.0	216.1	590.0	126.4	8.8	157.4	6.0
Dow Chemical	1,881.0	2,272.0	2,267.0	5.0	257.0	72.0	2.9	14.0	25.9
Du Pont	6,740.0	7,772.0	12,333.0	4,561.0	1,375.0	(485.0)	NM	40.1	43.3
Eastern Air Lines	1,566.5	1,632.2	1,218.0	-414.1	149.5	90.9	16.4	33.2	NM
Eastman Kodak	3,662.0	4,656.0	6,102.0	1,446.0	893.0	(130.0)	NM	26.6	54.0
Eaton OP	710.4	801.0	943.5	142.5	178.0	9.8	4.4	31.1	61.3
Eaton UP	131.7	142.2	68.2	-74.0	-	-	-	-	-
Exxon	3,111.0	3,541.0	4,764.0	1,223.0	880.0	(105.0)	NM	6.4	9.8
Ford OP	6,353.5	7,191.4	9,340.3	2,148.9	1,666.0	403.7	7.1	6.5	29.5
Ford UP	6,648.4	6,724.6	6,082.5	-642.1	-	-	-	-	-
FPL Group	471.7	695.2	1,213.8	518.6	168.3	(2.3)	NM	10.3	14.4
GenCorp	1,231.0	1,255.0	1,380.0	125.0	139.0	9.0	11.4	112.2	NM
General Dynamics OP	2,451.4	2,766.8	3,259.3	492.5	379.8	70.0	15.6	89.6	127.5
General Dynamics UP	128.0	128.0	106.0	-22.0	-	-	-	-	-
General Electric	14,073.0	15,473.0	21,502.0	6,029.0	2,261.0	(227.0)	NM	19.4	76.2
General Motors OP	13,611.9	15,112.0	1,932.4	3,820.4	56.1	517.7	9.6	1.2	36.2
General Motors UP	19,604.0	19,673.9	17,477.9	-2,196.0	-	-	-	-	-
General Public Utilities	637.8	843.2	885.4	42.2	105.2	35.3	11.1	13.8	31.5
GM Hughes	2,081.6	2,547.6	3,792.3	1,244.7	436.8	(76.5)	NM	32.1	27.6
Goodyear OP	132.1	156.1	156.6	0.5	157.9	51.7	12.9	1.8	6.5
Goodyear UP	1,038.6	1,131.0	864.9	-266.1	-	-	-	-	-
Grumman	1,430.7	1,655.3	1,934.9	279.6	160.8	23.8	21.6	75.4	174.0
GTE	3,900.0	5,781.0	9,074.0	3,293.0	1,300.9	(26.2)	NM	29.2	41.1
John Hancock	426.4	648.0	743.0	95.0	-	22.3	11.5	2.5	39.0
Hercules	692.0	787.4	1,124.9	337.5	124.2	(27.5)	NM	33.8	33.8
Honeywell OP	1,314.7	1,481.4	1,550.9	69.5	88.5	40.6	-10.3	30.5	75.9
Honeywell UP	396.3	400.9	310.4	-90.5	-	-	-	-	-
IBM	10,473.0	15,466.0	19,598.0	4,132.0	2,058.0	(55.0)	NM	26.8	26.5
Inland Steel	1,127.0	1,233.0	1,488.0	255.0	167.0	(21.0)	NM	50.9	72.3
International Paper	1,193.0	1,302.0	1,956.0	654.0	183.0	(58.0)	NM	20.7	26.2
ITT	1,676.0	1,975.0	1,926.0	-49.0	245.0	146.0	15.2	4.6	20.9

Definitions:

ABO: Accumulated benefit obligation. The value of all benefits earned to date.
PBO: Projected benefit obligation. A measure of the liability for accumulated service reflecting future salary increases.
NM: Not material
OP: Overfunded plan
UP: Underfunded plan

*Adjusted for benefit payments in some cases

Source: Companies' 1988 annual reports; all dollar figures are in millions

Funded status slipped in 1988

By Curtis Vosti

The health of the nation's largest defined benefit pension funds remained relatively strong in 1988, *Pensions & Investment Age*'s survey of annual reports shows.

Slightly more than 71% of the plans in the *P&I Age* Corporate Top 100 were fully funded in 1988, meaning they had more assets than projected benefit obligations, down from more than 72% in 1987.

The total number of plans listed each year is more than 100, because pension accounting rules require companies with more than one plan to list each separately where one fund is underfunded. Typically, a firm with more than one plan has one overfunded and one underfunded plan.

(In a slight variation from last year's survey, the 100 companies used this year were the largest in terms of defined benefit plan assets as determined by *P&I Age*'s annual survey of the nation's largest 200 employee benefit funds; last year, the 100 companies were the tops in total pension assets.)

The financial health of corporate pension plans largely has been the result of the high investment earnings and low inflation of the 1980s, according to David Kudish, managing director of Stratford Advisory Group Inc., a Chicago pension consultant. But Mr. Kudish and others are concerned continual government regulation could have a negative effect if and when those investment returns and inflation rates take a turn for the worse.

The average company in the Top 100 had $2.9 billion in accumulated benefit obligations, $3.4 billion in projected benefit obligations and $3.9 billion in assets. (Companies with more than one plan had their obligations and assets combined).

The five top funded plans, measured in terms of plan assets in excess of projected benefit obligations, are sponsored by: American Telephone & Telegraph Co., New York; E.I. du Pont de Nemours & Co., Wilmington, Del.; General Electric Co., Fairfield, Conn.; General Motors Corp., Detroit; and IBM Corp., Armonk, N.Y.

William F. Quinn, president of AMR Investment Services Inc., Fort Worth, Texas, said he thinks corporate pension plans are in even better shape than the PBO/asset comparison indicates.

Mr. Quinn believes a better measure of the plans' health is comparing the accumulated benefit obligations with the plan assets. He thinks using the projected benefit obligations doesn't take into account future contributions.

AMR Corp., AMR Investment's parent company, had $236.9 million more in projected benefit obligations than plan assets; but using the ABO/assets comparison, AMR had $90.5 million more assets than pension obligations.

"If you eliminate a defined benefit plan, those projected obligations would go away tomorrow," Mr. Quinn said. "With that impetus, it is very likely the PBO comparison is not realistic. If you

used ABO, most plans would be fully funded."

Mike Johnston, an actuary and partner with Hewitt Associates, Lincolnshire, Ill., pointed out, however, that although both methods are valid, the PBO is more reflective of the ongoing nature of pension plans, while the ABO would be more relevant if the plan were to be terminated.

Changes in reporting standards in 1989 require a booking of unfunded ABO liabilities in excess of the pension liabilities already recorded.

New regulations also will require that companies with underfunded plans meet the liabilities more quickly than they had in the past, Mr. Johnston said. That requirement is just the latest imposed by the government and the Financial Accounting Standards Board.

For instance, the 1987 requirement that set a full-funding limit at the lesser of actuarial liabilities or 150% of accrued liabilities caused many plans to use bond immunization to meet ongoing costs, he said. This can be harmful to the health of corporate plans if the markets turn down.

"If there is a recession, that 50% cushion could evaporate overnight," said Steve Vernon, a consulting actuary for The Wyatt Co. in Los Angeles.

John Turner, deputy director of the research office of the Department of Labor's Pension and Welfare Benefits Administration, said the office has contracted a study to determine the effects of the full-funding limits.

FASB 87, which requires either excess pension assets or unfunded liabilities be shown on the balance sheet, "probably has created more focus on the liability side that many corporations didn't have before," said Victor Bell, managing director of Lowry Consulting Group Inc., Atlanta.

Gary Pines, a principal in the Chicago office of Towers Perrin, suggests current surpluses could go away as the government continually tinkers with pension legislation.

A current proposal from Rep. Dan Rostenkowski, D-Ill., would allow companies to use pension surpluses to fund post-retirement medical benefits, while another proposal, by Sen. Howard Metzenbaum, D-Ohio, would limit what the companies could do with the surpluses, Mr. Pines said, thus exerting more impetus for firms to change to defined contribution plans from defined benefit plans.

"You may see the number of firms with more assets than projected benefit obligations drop to 50% or 40%," he said.

Another actuarial trend affecting pension plans is the increasing use of the projected unit credits cost method from entry-age normal cost method, Mr. Vernon said. The projected unit credits method has the tendency to spread costs further into the future, while the entry-age normal method tended to maximize contributions and tax deductions.

Investment gains last year were large enough to have 28 plans reporting pension income. Du Pont's was highest — $485 million.

AT&T reported the largest return on its pension assets, earning $3.4 billion. Other top returns included GE, with $2.3 billion; IBM, with $2.1 billion; and one of Ford Motor Co.'s plans, with a $1.7 billion return.

Four plans — AMR, Armco Inc., Parsipanny, N.J.; Tenneco Inc., Houston; and United Technologies Corp., Hartford, Conn. — reported a loss on pension assets. Spokesmen for Armco and AMR said the figures reflected an adjustment for benefit payments. ■

P&I Age Corporate Top 100

Company	ABO	PBO	Plan assets	Plan assets in excess of PBO	Actual return on plan assets*	Net periodic pension expense (income)	Pension expense as a % of adjusted net income	Plan assets as a % of corporate assets	ABO as a % of shareholders equity
James River OP	564.4	564.7	596.0	31.3	11.4	14.6	6.5	11.9	30.1
James River UP	382.9	412.4	313.3	-99.1	-	-	-	-	-
Johnson & Johnson	681.0	878.0	1,022.0	144.0	123.0	33.0	3.3	14.4	19.4
K mart	694.0	871.0	986.0	115.0	126.0	25.0	3.0	8.1	13.9
Eli Lilly	823.9	1,092.4	1,315.8	223.4	183.7	20.2	2.6	25.0	25.5
Litton	549.1	627.3	913.6	286.3	359.0	10.0	5.6	18.0	46.7
Lockheed	3,097.0	3,538.0	4,981.0	1,443.0	541.0	7.0	1.1	75.0	125.1
Martin Marietta	1,051.3	1,334.0	1,987.8	653.8	132.8	39.7	10.0	59.9	87.6
McDonnell Douglas	2,911.0	3,334.0	5,099.0	1,765.0	770.0	(93.0)	NM	42.9	91.4
Metropolitan Life	866.0	-	1,448.0	-	-	-	0.0	1.5	24.9
Minnesota Mining	1,525.0	1,753.0	2,173.0	420.0	217.0	0.0	0.0	24.4	27.7
Mobil	1,717.0	2,194.0	2,224.0	30.0	228.0	50.0	1.8	5.7	10.9
Monsanto	2,312.0	2,640.0	3,169.0	529.0	340.0	4.0	0.7	37.5	60.8
Navistar OP	25.0	27.0	60.0	33.0	230.0	83.0	25.4	2.4	2.9
Navistar UP	2,126.0	2,158.0	1,751.0	-407.0	-	-	-	-	-
NCR OP	698.5	815.8	1,161.9	346.1	134.0	(6.7)	NM	24.6	31.2
NCR UP	20.5	26.2	0.1	-26.1	-	-	-	-	-
North American Philips	607.3	748.2	1,025.0	276.8	138.6	(10.7)	NM	29.9	38.4
Northrup OP	1,269.1	1,566.3	2,263.3	697.0	223.0	4.3	4.0	72.1	126.5
Northrup UP	32.9	37.6	8.0	-29.6	-	-	-	-	-
NWA OP	553.4	741.7	822.2	80.6	117.5	28.1	17.2	18.8	33.9
NWA UP	353.3	366.9	316.3	-50.6	-	-	-	-	-
NYNEX	7,722.0	9,267.0	11,539.0	2,272.0	1,488.0	31.0	2.3	45.5	82.0
Pacific Telesis	6,089.0	7,159.0	8,898.0	1,739.0	1,147.0	130.0	9.9	42.0	75.3
J.C. Penney	758.0	1,001.0	1,164.0	163.0	125.0	(5.0)	NM	9.5	19.2
PG&E	1,931.7	2,721.0	2,535.7	185.3	323.1	103.5	62.5	12.0	28.0
Philadelphia Electric	747.7	1,046.7	1,163.1	116.4	134.6	7.1	1.2	9.8	20.8
Philip Morris	2,709.0	3,507.0	4,353.0	846.0	372.0	26.0	1.1	11.8	35.3
PPG OP	179.3	187.0	245.4	58.4	112.1	(4.0)	NM	4.8	8.0
PPG UP	663.1	812.6	775.1	37.5	-	-	-	-	-
Prudential	2,125.0	2,814.0	4,159.0	1,345.0	61.0	129.0	13.5	2.7	56.4
Raytheon OP	1,010.8	1,342.9	1,564.1	221.2	258.7	58.4	10.7	33.0	47.7
Raytheon UP	429.0	431.8	403.8	-27.9	-	-	-	-	-
Rockwell International OP	3,971.4	4,511.7	5,776.7	1,265.0	551.8	(135.9)	NM	62.7	107.5
Rockwell International UP	615.1	639.4	445.7	-193.7	-	-	-	-	-
Sears, Roebuck OP	2,912.0	3,793.0	4,621.0	828.0	523.8	72.9	4.8	5.9	20.7
Sears, Roebuck UP	213.0	269.0	181.0	-88.0	-	-	-	-	-
Shell Oil	2,364.0	2,701.0	3,173.0	472.0	388.0	47.0	3.7	11.7	15.4
SoCal Edison	973.7	1,409.1	1,326.6	-82.4	133.7	46.1	5.7	8.9	19.2
Southern Co.	930.0	1,377.0	1,976.0	599.0	223.0	38.0	4.3	10.0	13.9
Southern New England Tel.	861.8	983.1	1,426.8	443.7	194.2	(9.3)	NM	46.5	74.6
Southwestern Bell	3,893.8	3,930.9	6,189.3	2,258.4	718.7	56.0	5.0	29.5	45.8
Sun Oil OP	882.0	1,009.0	1,178.0	169.0	175.0	(8.0)	NM	13.7	26.5
Sun Oil UP	151.0	164.0	54.0	-110.0	-	-	-	-	-
Teledyne	666.1	791.1	1,425.7	634.6	99.3	(34.7)	NM	45.8	31.1
Tenneco OP	1,263.0	1,536.0	2,221.0	685.0	-163.0	(57.0)	NM	12.8	40.0
Tenneco UP	316.0	318.0	200.0	-118.0	-	-	-	-	-
Texaco	964.0	1,281.0	1,323.0	42.0	153.0	46.0	3.4	5.0	11.9
Textron OP	1,350.5	1,557.3	2,059.4	502.1	210.3	5.4	2.3	16.4	56.6
Textron UP	241.7	249.3	170.1	79.2	-	-	-	-	-
Travelers	924.0	1,266.0	1,299.0	33.0	150.0	9.0	8.0	2.4	20.2
TRW	1,379.0	1,698.0	1,860.0	162.0	174.0	26.0	9.1	41.9	3.3
UAL OP	1,135.8	1,478.9	1,653.3	174.4	183.4	73.8	6.2	24.7	89.7
UAL UP	272.1	412.1	168.8	-243.2	-	-	-	-	-
Union Carbide	1,636.0	2,100.0	2,078.0	-22.0	225.0	36.0	5.2	24.6	89.1
Unisys OP	2,054.0	2,696.4	2,748.3	51.9	347.4	49.9	6.8	23.8	41.5
Unisys UP	87.8	92.4	45.6	-46.8	-	-	-	-	-
United Technologies OP	3,695.8	4,564.4	5,429.5	865.1	-158.3	(17.3)	NM	42.6	76.6
United Technologies UP	334.5	442.5	215.4	-227.1	-	-	-	-	-
United Telecom	532.2	740.2	1,085.7	345.5	113.6	(1.9)	NM	11.1	28.4
USX	7,551.0	7,856.0	8,564.0	708.0	1,002.0	(234.0)	NM	44.0	132.8
U S WEST	3,845.0	4,810.0	7,120.0	2,310.0	867.6	(47.1)	NM	31.8	49.4
Warner-Lambert	678.3	763.7	853.3	89.6	132.4	(21.3)	NM	31.6	67.9
Westinghouse	4,331.4	4,823.0	3,745.1	-1,077.9	366.1	101.3	11.0	22.1	114.1

Definitions:

ABO: Accumulated benefit obligation. The value of all benefits earned to date.
PBO: Projected benefit obligation. A measure of the liability for accumulated service reflecting future salary increases.
NM: Not material
OP: Overfunded plan
UP: Underfunded plan

*Adjusted for benefit payments in some cases

Source: Companies' 1988 annual reports; all dollar figures are in millions

INTERNATIONAL

U.S. firms' foreign business booms

By Leonard J. Hollie

U.S. money managers saw their assets from foreign institutional clients surge 37.5% during the past year, according to a survey by *Pensions & Investment Age*.

Investments for foreign institutions by the U.S. companies totaled $64.1 billion March 31, according to responses from the 47 large financial institutions responding to the survey.

The survey included only U.S. firms and excluded those whose principal businesses were outside the United States. Not all the firms believed to have foreign assets under management responded to the survey.

The amount the U.S.-based managers invest for their clients in the United States is a small part of the more than $790 billion these managers invest for clients worldwide.

Citicorp Investment Management, New York, with $18.4 billion invested for foreign clients, led the survey. The total represented a gain of almost 45% from the $12.7 billion under management for foreign institutions last year. Of the total, $8 billion was invested in the United States.

Chase Investors Management Corp., New York, with $6.9 billion invested for foreign clients, ranked second in the survey. Because Chase did not report the amount managed for non-U.S. investors in 1988, its rate of growth could not be determined, and its numbers weren't included in the data used to calculate the increase in foreign assets under management. Chase's assets, however, are included in the totals listed in this story and in the accompanying table.

Besides Citicorp, the firms with the largest gains in assets managed for foreign institutional clients included State Street Bank & Trust Co., Boston, which reported managing $1.93 billion, an increase of more than $1 billion from last year's $912 million; Rosenberg Institutional Equity Management, Orinda, Calif., which also gained just more than $1 billion; and Wells Fargo Investment Advisors, San Francisco, which gained $551 million.

A significant part of Citicorp's non-U.S. assets — $5.25 billion — was from foreign sovereign governments. Other U.S. investment managers also reported managing large amounts of assets for foreign governments. Chase managed $4.5 billion for sovereign governments; The Chemical Investment Group, New York, $1.7 billion; and State Street Bank, $1.5 billion.

Except for Citicorp, the top firms in terms of foreign business growth last year were those that offered indexed or highly quantitative approaches — Wells Fargo, State Street and Rosenberg Institutional Equity Management.

"We saw a growing demand on the part of foreign investors toward getting into some kind of indexed program," said Peter Braun, vice president and director of marketing at State Street. "We haven't seen a real big demand for indexing in one particular country. It's mainly a multicountry phenomenon."

Japan was the largest source of assets managed by U.S. managers, followed closely by the Middle East. Japanese institutions have given U.S. managers $13.5 billion to invest, while those in the Middle East have given them $13.3 billion. U.K. institutions were next with $8.2 billion.

Overall, however, foreign investors looked to the U.S. institutions mainly for active equity and fixed-income management. The U.S. managers had $23.4 billion in active equity accounts for foreign clients, $13.1 billion in active fixed-income accounts, $8.5 billion in real estate, $4.4 billion in passive equity accounts and a slight $10 million in passive fixed income.

Foreign clients, however, have been showing increased interest in fixed-income investing.

"They like the strength of the dollar and also because the U.S. has the highest real rates of return than any other country," said Robert Follert, Morgan Stanley Asset Management, New York, vice president and director of ERISA and tax-exempt marketing. "Countries that are concerned about the stability of their own currency are looking to get into fixed income in the United States."

Morgan Stanley shows a nearly

Continued on page 34

Foreign business

How assets are invested

	$ millions
Active equity	23,385.6
Passive equity	4,403.0
Active fixed	13,111.4
Passive fixed	10.0
Balanced*	13,183.5
Real estate	8,534.0
Venture capital	228.0
Cash	3,667.2
Other	9,190.6

* assets might be double counted in equity/fixed allocations

Source of assets by client

	$ millions
Pension funds	7,785.7
Insurance companies	11,193.4
Mutual funds	5,201.7
Corporations	3,911.0
Governments	16,764.5
Banks	2,471.7
Other	10,769.0

Source of assets by country/region

	$ millions
United Kingdom	8,212.1
Japan	13,575.9
Australia	3,604.2
Europe	6,004.3
Canada	2,731.7
Middle East	13,348.0
Other	8,662.8

Top U.S. managers of foreign institutional assets

Name	$ millions
Citicorp	18,373
Chase Investors Mgmt.	6,961
CIGNA	4,080
The Capital Group	3,255
The Yarmouth Group	3,105
Morgan Stanley Asset Mgmt.	2,805
Chemical Investment Group	2,700
Alliance Capital Mgmt.	2,440
Fischer, Francis, Trees & Watts	2,200
State Street Bank & Trust	1,930
Equitable Real Estate	1,611
CIC Asset Mgmt.	1,492
Corporate Property Investors	1,350
Wells Fargo Investment Advisors	1,317
Rosenberg Institutional Equity	1,301
Equitable Capital Mgmt.	1,284
Merrill Lynch Asset Mgmt.	1,076
Manufacturers Hanover	1,060
Schroder Real Estate Associates	775
First Boston Asset Mgmt.	685
Atlanta Capital Mgmt.	499
Batterymarch Financial Mgmt.	411
Scudder, Stevens & Clark	409
Dimensional Fund Advisors	379
Dewey Square Investors	330
Fayez Sarofim	291
Bernstein-Macaulay	250
Templeton, Galbraith & Hansberger	226
Mitchell Hutchins	218
Boston Co.	167
Miller, Anderson & Sherrerd	159
Templeton Investment Counsel	142
Lazard Feres Asset Mgmt.	135
Tyndall-Newport Mgmt.	105
Columbia Mgmt.	72
RXR Capital Mgmt.	64
Burgess Capital	60
BEA Associates	58
TSA Capital Mgmt.	58
GAMCO Investors	45
Harris Trust and Savings Bank	44
Oppenheimer Capital	43
Wellington Mgmt.	43
PCM International	39
Provident Capital Mgmt.	29
Marinvest	19
Massachusetts Financial Services	13
TOTAL	**64,108**

Europe already fruitful

By Curtis Vosti

GENEVA, Switzerland — Although many investors are eyeing the proposed consolidation of the economies of Western Europe as a key to opportunity, a Swiss banking firm contends the Continent already is "an underrated giant."

Despite having as many people as the United States and Japan combined, and a combined gross domestic product larger than that of the United States and almost twice that of Japan, European stock markets are rated much lower, with a total capitalization half that of the Japanese market.

"Actually, nothing could be further from reality than the hackneyed image of a hidebound, ossified Europe unable to control its destiny," according to a report from Lombard Odier & Cie, Geneva, titled "New Land of Opportunity."

The report is one of a series of the firm's Project Europe, a look at investment opportunities for Europe into the 21st century that provides an overview of European political and economic patterns and seeks to explain how they will change in the coming decade.

"While Europe is already doing well, it will do even bet-

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Funds catch on

Smaller investors looking abroad

By Margaret Price

International investing, once the purview of large U.S. tax-exempt institutional investors, is spreading to the midsize and smaller fund sector amid interest in, and concerns about, diversification.

While few, if any, consultants chart overseas investments by fund size, the data that are available show an unmistakable trend.

Commingled international funds — an investment vehicle often used by smaller funds — have been growing at an impressive clip. According to InterSec Research Corp., Stamford, Conn., commingled funds garnered about $16 billion, or roughly 30%, of the $53 billion in total international equity investments by tax-exempt institutions as of March 31. As of March 31, 1988, about $10.5 billion, or 26.9%, of the roughly $39 billion in total international equity investments by these institutions, went to commingled funds.

"A few larger funds also use (commingled funds), but largely they are used by small- to medium-size funds," said Duncan Fordyce, senior vice president of InterSec.

While there was some discrepancy among consultants, the small- and medium-size funds generally were considered those with total assets between $5 million and $200 million.

With the rising U.S. dollar, however, foreign investments have taken a riskier twist. A rising dollar reduces the value of assets denominated in foreign currencies.

Some consultants said the strength of the dollar might eventually dampen enthusiasm for foreign stock investments.

Joseph Scarella, a consultant at Wyatt Asset Services, New York, said he hasn't "seen any pull back" from foreign equity markets so far this year. "But in three months, if the dollar keeps strengthening, there could be evidence of some reluctance," he said.

Mr. Scarella and other consultants noted, however, that over the long term, currency differentials should become inconsequential, which presumably could help assuage long-term investors' fears.

The approximately $200 million endowment of the Rensselaer Polytechnic Institute, Troy, N.Y., found a way to reduce the dollar problem.

For its first investments outside the United States, the endowment decided to choose a global money manager, putting 10% of its assets with Capital Guardian Trust Co., Los Angeles. "Much less than half of that allocation was targeted for outside the U.S.," said David D. Gonino, the endowment's investment officer.

Rensselaer's global outlay is being handled through a separate account, not a commingled fund. "The vast minority of global money managers interviewed discussed commingled funds with

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Europe ready

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ter as the European Community's Single Market nears completion. But the landscape will be changed beyond recognition. Those who want to invest today in what Europe will become tomorrow had better have a good sense of direction," according to the report.

The five-part report makes the case for a consolidated Europe that "is in good shape economically and socially, much better than the United States and in many respects, . . . can hold its own with Japan."

Among the factors listed supporting this notion are that Europe already has begun to adjust to aging populations that are "a time bomb ticking away in many parts of the world;" the European savings rate is "more than high enough to finance very substantial domestic capital investments;" the Continent shows a steady and strong growth rate with success in curbing inflation and an unobtrusive small trade surplus; and it has a shrinking public sector, which could lead to smaller budget deficits and lower taxes.

"True enough, the time when Europe stood as the world's foremost political, industrial and financial power is long bygone," the report states. "But its decline has been arrested . . . Barely 20 years ago its companies emerged from the problem-ridden decades and rose to the challenge of welding the Common Market together."

As a result, "despite the twists and turns of recent years, real growth has been running at a steady 2% to 3% annually in Europe."

But as the 1980s evolved, the nations of Western Europe began to realize the idea of a unified Europe as revealed in the Common Market was "running out of steam," the report states. Hence, in 1985, the community issued a "White Paper" designed to plot a new course for economic interdependence.

Although the report states some of the measures set forth in that paper are mostly symbolic, such as the dismantling of intracommunity border checkpoints, there are three major categories of proposals that "will probably be very important indeed."

They are: the harmonizing of health and other technical standards; selective competition in public procurement contracts that will "revolutionize" previously sheltered industries such as telecommunications and public transportation; and the standardization of indirect taxes and the free circulation of capital, which will increase the mobility of people and companies.

"The remedy adopted has been both ambitious and down-to-earth," the report states. "Ambitious because it is aimed at achieving a genuine economic union at last and down-to-earth because one of the cornerstones is to be the creation of a single market spanning 12 and perhaps even 18 countries."

One of the beneficiaries of this endeavor will be the financial markets, the report states. The prediction is for a "quiet revolution," which has the aim of overcoming distribution problems caused by the fragmentation of consumers and producers by the numerous country borders.

Among the stages that will revolutionize financial services will be the abolishment of exchange controls by July 1990 and the operation of banks under a single license, which will lead to the rise of universal banks offering a full range of banking services.

"Regardless of EC membership, all of the economies and stock markets of Western Europe will benefit from the push for integration," the report states. Equity trading volumes and market performances should be bolstered because greater savings and the growth of pension plans and insurance coverage should generate "substantial" liquidity; the liberalization of financial services will broaden the markets and lead to the creation of new financial instruments; and there will be increased mergers and acquisitions and corporate financing activity. ■

U.S. firms

Continued from page 33

$1 billion drop in foreign assets managed in 1989, with a total of $2.8 billion, as opposed to $3.7 billion a year earlier. Mr. Follert said it is Morgan Stanley's policy not to comment on the decline.

He said Morgan Stanley is expanding its client base in Europe and Japan and is very interested in emerging countries as a new investment vehicle. The firm offers a Thailand fund, and is about to come out with a private placement in India.

Rosenberg Institutional Equity Management has concentrated on Japanese investors, setting up a joint venture in 1987 with The Nomura Group in Japan. Through its Tokyo subsidiary, Rosenberg Asset Management Ltd., Rosenberg invests in the United States money raised in Japan by Nomura. Narlis Fritz, partner and director of marketing, said by late summer or early fall, the firm expects to start a Japanese model for Japanese investors who want to invest in Japanese securities.

Rosenberg reported $1.3 billion in assets managed for foreign clients, an almost fivefold increase from 1988's $284 million.

"Our strategy is appealing to the non-U.S. investor," said Ms. Fritz. "It's a core equity product designed to outperform the benchmark indexes such as the S&P 500 or the Russell 3000 by 400 basis points a year." The firm had $5.2 billion under management worldwide as of March 31. ■

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Trades show

Continued from page 3

tunity cost of not being able to execute all limit trades. What's more, limit orders sometimes generate market impact, as other investors anticipate purchases.

Application of the two most widely used measurement systems — Abel/Noser's and SEI Corp.'s — illustrated these problems.

Abel/Noser's cost methodology compares the cost of a trade to the volume-weighted average price on the day the trade was executed. Because RJR systematically tried to buy underperforming stocks at or near the bid, it probably bought many stocks below the weighted average, the study said.

At the fund's request, Abel/Noser analyzed the trades and found, using the 88 New York Stock Exchange-traded stocks in the portfolio, and found RJ! made a profit of 5 cents per share or 28 basis points on its trades.

"Of course, this analysis masks the very real market impact and adverse selection that we actually experienced," according to the Kidder study.

A system based on comparing the transaction price with the closing price on the day after the trade date, devised by SEI, Wayne, Pa., was more accurate, the authors found, although that system still understated costs.

Using post-trade returns adjusted for market movement for each stock revealed stock trading cost 45 basis points measured one day after the trade, although reaching 186 basis points going 10 days out. While this system might have helped RJR and Kidder catch the dogs the fund had bought, SEI couldn't track the opportunity cost of not purchasing star performers, the study said.

Instead, the authors used an "implementation shortfall" system described by Professor Andre Perold of Harvard University. Under that system, a "paper portfolio" containing the entire 250-stock list was created at the onset; the difference in performance between the paper portfolio and the real portfolio reflects market impact, adverse selection and changes in the bid-ask spread.

In addition, the real portfolio's performance was adjusted for price changes in the Russell 2000 index while RJR was buying.

The real portfolio underperformed the paper portfolio by 213 basis points, net of market movement. (The cost was only 173 basis points if the aggressive buying in the last two weeks of trading is eliminated.)

Compared with an estimated cost of 300 basis points of doing the trade conventionally, patience paid off, improving performance by 87 basis points, the study said. That does indicate savings can be achieved through patient trading — although not nearly as much as some large investors suggest.

The study's final conclusion, however, contravened the conventional wisdom that all transaction measurement systems are flawed, and thus, it doesn't matter which system is used. Clearly, a cost of 213 basis points is far different from a profit-making 5 cents per share, the authors wrote.

"If Abel/Noser's (measurement) were the true cost, we would just keep churning our Russell 2000 account forever," said Robert Shultz, RJR's vice president-pension asset management, who also worked on the study.

Eugene A. Noser Jr., president of Abel/Noser, questioned whether RJR actually was providing liquidity to the market because the trades generally were very small, often in lots of several hundred, while the entire portfolio was only 600,000 shares.

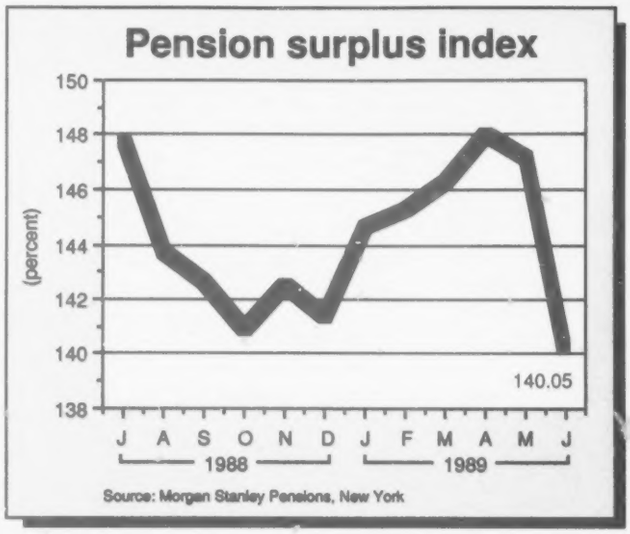
If RJR had purchased all of a given stock at the price of the close of bidding the night before the trade was executed, it would have saved $80,000 in trading costs, he said. Using the average volume-weighted price instead would have generated savings of $40,000, he added.

"You can't move the stock on a 500-stock order," Mr. Noser said.

Mr. Bodurtha replied, "I think we were dealing with an extraordinarily illiquid basket of stocks."

In addition, Mr. Noser said RJR's drawn-out method of building the portfolio — which took 67 trading days — was not reflective of actual trading practices.

But Paul Brakke, a vice president at Bankers Trust Co.-Investment Management Group, New York, refuted that point. "We've set up funds that have an even lower capitalization than the Russell 2000, and it's taken almost three months," he said. "The bottom line is, it's excruciatingly expensive." ■



Indexing

Continued from page 2

Boston, which lost $1.25 billion in indexed assets under management, had one public pension fund client switch $1.6 billion in fixed-income indexed assets into active management; Dimensional Fund Advisors Inc., Santa Monica, Calif., lost $1 billion in indexed fixed-income assets when a client switched to an active management approach; and Mellon Bond Associates, Pittsburgh, reported it lost $700 million in fixed-income indexed funds when a public fund redeployed some of its assets into active management.

But the overall, long-term logic behind pension fund investing in indexed funds is almost irresistible, according to the technique's supporters: The sheer size of the assets needing investment practically guarantees a spread of stock and bond investments that will mimic the broad indexes.

"Eventually we'll all get backed into a corner and we'll all be index managers if we're still expected to outperform the market, whether we like it or not," said Anthony Santosus, assistant vice president for quantitative analysis at Putnam.

In other changes in the business of indexed money management, Wells Fargo Investment Advisors, San Francisco, will become part of a joint venture with Nikko Securities Co. Ltd., Tokyo. Wells Fargo managed $59.4 billion in indexed funds as of May 31, up from $54.7 billion Nov. 30.

Boatmen's Trust Co., St. Louis, acquired Centerre Trust Co., also of St. Louis, at the end of 1988. Boatmen's managed $425 million in indexed funds May 31. Centerre had reported $415 million as of Nov. 30.

Also, MacKay-Shields Financial Corp. transferred its index fund business to Monitor Capital in late 1988. Monitor now manages $116 million in equity and fixed-income index funds.

Kiene Wooters and Associates Inc., Minneapolis, which manages $67 million in indexed funds, changed its name to the Clifton Group in April. ■

Funds seek

Continued from page 2

president of Callan Associates Inc., San Francisco, pointed out many pension fund sponsors don't use consultants to help them select indexers; consultants' services are needed more for evaluation of active managers, she said.

Robert Hunley, senior vice president of DeMarche Associates Inc., Kansas City, said his firm is not a big advocate of indexing, but noted some of the interest in quantitative strategies is an outgrowth of indexing. He sees a bit of a move toward fundamental investment styles. The firm also has done several searches for small-capitalization equity managers, he said.

Among the equity hirings reported in *P&I Age* in the past quarter, at least three were specifically for small-cap.

The apparent trend toward active management in the past few quarters indicates a possibility that the market for "plain vanilla" indexing is saturated, while specialized indexing continues to grow.

For instance, the one area where passive management was a major draw during the quarter was international. Of the $118 million reported for international hirings, $71 million was for indexed or passive strategies. Almost all of that $118 million also was for equity strategies, the exception being a $13.5 million international balanced account.

The $118 million was lower than amounts reported for international in several recent quarters, but it does not include seven manager hirings for undisclosed amounts by the $20 billion Wisconsin Investment Board, Madison. Three managers were selected for international equities, four for bonds. They will be funded gradually, with the board's total commitment to international eventually reaching $1 billion.

Other hirings reported in the quarter included $229.5 million for balanced management; $35.8 million for guaranteed investment contracts; $10 million for bankruptcy debt; and $7 million for cash management. ■

Leading index fund managers

($ millions - as of May 31)

Company	Total	Domestic equity	Domestic fixed	Int'l equity	Int'l fixed
Wells Fargo	59,357	37,865	18,400	3,021	71
Bankers Trust	29,524	26,503	2,401	620	0
Mellon Capital	23,850	18,765	4,580	505	0
State Street Bank	21,111	12,900	1,980	6,220	10
ANB Investment[1]	9,400	NA	NA	NA	NA
Alliance	6,648	5,955	20	673	0
GE Investment	5,860	5,860	0	0	0
Boston Co.	5,101	3,424	1,445	232	0
Mellon Bond	5,100	0	5,100	0	0
Dimensional Fund	4,592	4,187	0	405	0
Manufacturers Nat'l/Detroit	4,092	4,071	21	0	0
Wilshire	3,668	3,668	0	0	0
Lincoln Capital	3,200	0	3,200	0	0
T. Rowe Price	2,934	265	2,669	0	0
Chase Investors	2,777	1,486	372	919	0
Lehman Mgmt.	2,200	0	2,200	0	0
Prudential	1,985	697	1,027	261	0
Sears	1,885	1,691	0	194	0
Northern Trust[2]	1,659	1,155	463	30	11
Vanguard	1,635	1,547	88	0	0
Chancellor Capital	1,230	1,150	80	0	0
BEA Associates	1,146	1,146	*	0	0
Security Capital	1,050	0	1,022	0	28
Putnam	900	0	900	0	0
WR Lazard	860	0	860	0	0
Axe Core	744	477	0	267	0
Mitchell Hutchins	717	326	391	0	0
Bernstein-Macaulay	708	708	0	0	0
Travelers	693	327	148	195	23
NCNB Texas	604	604	0	0	0
Harris Trust	500	300	200	0	0
ASB Capital	494	494	0	0	0
Capstone Asset	470	470	0	0	0
Boatmen's	425	407	18	0	0
Boston Int'l	423	0	0	423	0
Fiduciary Trust	400	0	400	0	0
First Wisconsin	379	99	280	0	0
Fidelity	360	23	337	0	0
Aetna[3]	334	262	72	0	0
Associated Capital	294	186	108	0	0
Bear, Stearns	260	0	260	0	0
Todd Investment	240	0	240	0	0
NBD Bancorp	198	198	0	0	0
Old Kent Bank	138	138	0	0	0
Western Asset	123	0	93	0	30
Metropolitan Life[1]	117	117	0	0	0
Monitor	116	77	39	0	0
Chemical	80	0	80	0	0
Advanced Investment	75	75	0	0	0
Clifton	63	44	19	0	0
	210,719	**137,667**	**49,513**	**13,965**	**173**

[1] as of Dec. 31, 1988
[2] as of March 31
[3] as of June 30
* less than $500,000

ESOPs' future

Continued from page 3
duces the taxes of banks and other financial institutions and improves the financial statements of corporations. In many cases, these transactions provide little, if any, benefit for employees."

Following Mr. Rostenkowski's June 6 bombshell, investment bankers pressed their clients to establish ESOPs, fearing Congress might move to repeal or restrict dividend deductibility as well.

As a result, by the time repeal of dividend deductibility was proposed five weeks later, at least 24 companies had filed the necessary paper work or committed to setting up ESOPs, involving more than $5 billion in securities. Companies that squeezed through this window included Xerox Corp., Delta Air Lines Inc., Sara Lee Corp. and GTE Corp.

Through July 10, more than $17 billion in new ESOPs were set up by major corporations this year, according to the National Center for Employee Ownership, Oakland, Calif.

But the House proposal was changed abruptly July 13. In a closed meeting, the Ways and Means Committee carved out a gaping exception for firms that filed between June 6 and July 10. Under an amendment by Rep. Richard T. Schulze, R-Pa. the tax committee delayed the effective date of repealing the 50% interest exclusion to July 10 from June 6.

The House panel also approved an amendment sponspred by Rep. Beryl Anthony Jr., D-Ark., which retained both the partial-interest exclusion and the dividend deductibility for ESOPs that hold at least 30% of the sponsoring employer's stock.

The Anthony amendment primarily aids private firms; few public companies put this much of their stock into ESOPs because of the expense, contribution limits, stock-exchange rules and concerns about liquidity. Also, some executives might fear employees will tender their shares if an attractive offer is made.

ESOP proponents will try to counter any efforts by the Senate to restrict dividend deductibility and eventually will try to eliminate the provisions in conference.

The dividend deductibility rule received an important boost from the Treasury Department July 19, at a hearing held by two Senate finance subcommittees.

Dana Trier, acting deputy assistant secretary for tax policy, told the hearing the partial-interest exclusion has proven to be too expensive to the government but warned against repealing the dividend deductibility rule. "We are leery about taking away two major benefits from ESOPs at the same time," he said.

Mr. Trier added, however, the tax benefits from dividend deductibility need to be better targeted to promote "meaningful ESOP participation." Thus, the Treasury Department does not oppose the Ways and Means ESOP changes because the tax benefits would be limited to companies whose ESOPs own at least 30% of the employer stock.

ESOP advocates also hope to lower the 30% threshold contained in Mr. Bentsen's bill to 20% or lower, because that level is much more attainable for public companies. Rumors are circulating some senators may seek to knock the threshold to 15%.

Advocates also want to kill a provision in the bill that would require ESOPs with 30% ownership to provide pass-through voting to participants.

Eliminating that provision, which affects privately held companies — pass-through voting already is required of public companies — is deemed crucial because owners of companies are leery of handing voting control to employees when ESOPs are first established and because lenders may blanch at giving credit if management could be voted out, said David Binns, executive director of the ESOP Association, Washington.

A push also is emerging to reverse the July 10 extension sponsored by Mr. Schulze. The Schulze amendment "gives a windfall to lenders and to companies aware of the proposed bill but willing to proceed anyhow," Paul J. Mazzilli, principal at Morgan Stanley & Co. Inc., New York, wrote Sen. Robert J. Dole, R-Kan., the ranking minority member of the Senate Finance Committee and sponsor of another ESOP bill.

The cost of delaying the effective date might exceed the cost of retaining dividend deductibility, he added.

Sen. David Pryor, D-Ark., who chairs the Senate Finance subcommittee on private retirement plans, indicated he is studying the trade-off between the extended transition rules and "long-term" ESOP incentives, such as the dividend deductibility rule. ■

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Bill hikes role

Continued from page 1
Higgins & Co., New York.

But a United Auto Workers official said employers are "crying wolf." Alan Reuther, UAW associate general counsel, said, "I think it's nonsense. You've had jointly trusteed plans for years on the multiemployer side, and some on the single-employer side and they don't get terminated."

Other budget bill-related actions affecting retirement plans included:

- The House Ways and Means Committee adopted a proposal to permit employers to transfer surplus pension assets exceeding 140% of current liabilities to retiree health accounts during 1990 and 1991.

The provision may never be used, experts said, because it requires employers to vest all participants' pension benefits and *purchase annuities to cover them* in order to effect a transfer.

The Ways and Means provisions also would limit deductions and contributions for retiree health and pension expenses for companies that transfer surplus assets.

The committee voted to reverse an Internal Revenue Service ruling permitting employers to fund 401(h) retiree medical accounts even if their pension plans are at the full-funding limit.

- The House Education and Labor Committee approved, in a party-line vote, an amendment to its budget-reconciliation bill that would prohibit all reversions of surplus pension assets to employers. But pension assets exceeding 150% of current liabilities could be shifted to a retiree health trust under the amendment.

Participants would be vested immediately in their medical benefits. Employers would be barred from reducing health benefits for this group in the future, and from three years prior to the transfer.

The panel passed the provisions to ensure it has a role in retiree health and asset reversion issues.

- The Senate Labor and Human Resources Committee, by a vote July 20 of eight to seven, attached key provisions of Ohio Sen. Howard Metzenbaum's asset reversion bill, S. 685, onto its own budget-reconciliation bill.

The Senate labor committee's proposal would not ban reversions but would permit employers to recapture surplus assets only where there is a replacement plan and after leaving a cushion of assets based on projected benefit obligations and providing a one-time cost-of-living adjustment.

Opponents, including the Bush administration, argue that would leave little or nothing for employers and that the bill would encourage poor funding practices.

In addition, the Senate panel adopted a provision permitting the transfer of surplus assets to retiree health accounts similar to that in the House bill. Also attached to the panel's budget-reconciliation measure, the Senate bill would require the Department of Labor study the need for vesting, accrual and portability rules for such health benefits.

- Both House and Senate labor committee bills rely on imposition of new user fees ranging between $100 and $1,000 for filing annual reports, summary plan descriptions and other retirement plan-related filings, and a stiff $200 per participant tax for plans that are terminated.

- The House Labor Committee also approved H.R. 1661, the House equivalent of S. 685, while the Senate Labor panel deferred action on S. 685. The Joint Committee on Taxation and the Congressional Budget Office estimated those bills would cost the government $1.7 billion during the next five years.

But it was the Visclosky amendment that took the employee benefits community by surprise.

The amendment stemmed from concerns pension assets have been used to finance takeovers, either through the termination of overfunded plans by corporate raiders or through pension investments in junk bonds and other instruments. Workers should have a say in such matters, Mr. Visclosky has argued.

The amendment provides unions would pick their representatives, while salaried participants would elect their trustees in a secret ballot.

"The concept of joint trusteeship turns fiduciary responsibility into a popularity contest, where current law requires the highest possible standards of investment responsibility," said Mark Ugoretz, executive director of the ERISA Industry Committee, Washington.

While pension experts noted the Visclosky amendment would cause sweeping changes in plans' operations, several expressed doubt the amendment ever would be passed by the full Congress.

Corporations were disappointed with the retiree health provisions included in the Ways and Means tax bill. A Department of Treasury official said it favored the proposal because of its narrow approach but the annuitization requirement was unnecessary. ■

Debate

Continued from page 3
sarily an economical way to finance similar employee benefits or an effective way to motivate employees.

Mr. Wolfson, who collaborated with Myron Scholes, professor of finance and business, also at Stanford, in analyzing ESOPs, attributes the predominance of ESOPs to either a corporate perception of their power as an anti-takeover device or to misperception of their potential economic and productivity benefits.

Many companies downplay, or reluctantly concede, their ESOPs are anti-takeover devices, especially in light of a Polaroid Corp. ruling that allowed establishment of an ESOP in the midst of a struggle for control of a company because a Delaware court decided the plan enhanced both employee compensation and shareholder value.

In terms of the tax advantages, Mr. Wolfson agrees with the analysis of Howard A. Freiman, vice president at Fidelity Management Trust Co., Boston, who concludes leveraged ESOPs often might provide fewer tax advantages than unleveraged ESOPs or other defined contribution plans providing the same benefits. (*Excerpts from Mr. Freiman's analysis appear on page 27.*)

Among his major assertions criticizing the headlong rush to ESOPs, Mr. Freiman said in an interview, "For a leveraged ESOP, the stock price at the time of the ESOP's establishment determines the tax deduction for allocating stock to employees' accounts. However, for other defined contribution plans, the stock's current market value determines the tax deduction. Thus, in a rising stock price environment, a leveraged ESOP will often receive a significantly smaller tax deduction for providing an equal amount of employee benefits."

Mr. Mazzilli, who heads Morgan Stanley's ESOP financing group, is familiar with Mr. Freiman's argument and agrees unleveraged ESOPs may offer some better economic benefits than leveraged ESOPs. "In terms of a rising stock price (as Mr. Freiman assumes), the treasury purchase is probably better than a leveraged ESOP."

But Mr. Mazzilli said such unleveraged ESOP allocations, issued from treasury shares, "hurts a company's credit rating more, because you have no obligation to reissue the shares."

"A leveraged ESOP is looked on more favorably by (credit) rating agencies because it shows a specific commitment to pay down debt," he added.

In regard to non-economic terms, among other advantages, he said employees may influence the voting of unallocated leveraged ESOP shares. Treasury shares, he added, have no vote.

While ESOPs might be effective in motivating top management, Mr. Wolfson believes that for many employees, owning company stock might have only an indirect effect. He said more direct incentives, such as bonuses, might have a more profound effect.

The downgrading of Colgate-Palmolive's rating for its senior debentures to A2 from A1 by Moody's shows an ESOP's economic advantage might be more complex to determine.

"It was felt the ESOP program was too large for the company's size," said Moody's Ms. Gaforek. The ESOP debt will raise Colgate-Palmolive's total debt to capital ratio to 55% from 37%, she said. By contrast, she said the $1 billion ESOP announced earlier this year by Procter & Gamble Co., Cincinnati, although much larger in terms of absolute dollar value, raised its ratio to a more manageable 40% from 31% and had no effect on its debt rating.

Ms. Gaforek said Colgate-Palmolive's ESOP also reduces the company's financial flexibility. By setting up the ESOP, she said, the company will be shifting a large part of its future employee benefit costs to a fixed obligation from a contingent liability.

By contrast, Standard & Poor's Corp., New York, has kept Colgate-Palmolive's senior debt rating at A+ since 1987.

"The way we view this particular ESOP is that we consider this a pre-funding of an employee benefit," said Angela Uttaro, assistant vice president in Standard & Poor's Ratings Group of McGraw-Hill Financial Services Co., New York.

"The plan does reduce financial flexibility, if you're looking at a company on the financial edge," she said, adding she doesn't view Colgate-Palmolive as on the edge.

In terms of creating a fixed obligation, she said Colgate-Palmolive had never reduced its employee benefits so for all practical purposes had a fixed obligation.

Colgate-Palmolive executives were unavailable for comment. ■

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PENSIONS &

InvestmentAge

The newspaper of corporate and institutional investing

Canada, U.S. ease financings

By Marcia Parker

The Securities and Exchange Commission and a Canadian counterpart have proposed a system that will make it easier and less costly for issuers in both countries to make cross-border securities offerings, facilitating the flow of capital and broadening investment opportunities.

The proposed multijurisdictional disclosure rules represent the first concrete steps taken by North American countries to eliminate the sometimes formidable barriers facing issuers who raise capital or make exchange or cash tender offers to investors outside their home country and the investors who want to buy their securities or participate in the exchange or tender offers.

Under the proposal between the SEC and the Ontario Securities Commission, U.S. issuers that meet certain tests would be able to make public offerings and tender offers in Canada using disclosure documents prepared according to SEC requirements. Eligible U.S. issuers of investment-grade debt or preferred stock would have a market value of at least $150 million and $400 million in the case of other securities.

The periodic financial reports U.S. issuers have to file with the SEC also would be accepted in Canada to meet its continuous reporting requirements. Although Canada does not have a concept of shelf registration, under the system, procedures will be proposed by the OSC to accommodate U.S. issuers making shelf offerings.

Like the SEC, the OSC is the Canadian regulatory agency overseeing corporate issuance and other capital market activity.

Continued on page 42

Rescuing Wall Street

Investors up commissions

By Joel Chernoff

Suffering losses from brokerage activities, Wall Street is receiving help from an unexpected quarter: pension funds and their money managers.

In the face of declining liquidity and increasing unwillingness by brokers to supply capital to the market, institutional investors are starting to realize brokerage firms must profit on their trades for the benefit of all concerned.

"It doesn't make sense to have a brokerage industry that doesn't make money," said Jerry Hartman, managing director at Scudder, Stevens & Clark, New York.

A combination of efforts by Wall Street firms and institutions are leading to higher commissions for trades, especially for those in which brokers use their own capital, such as block trades.

In one instance, Union Carbide Corp.'s investment management unit told brokers it would be willing to increase commission levels a penny or two per share, from an average of 6 cents per share, for all trades.

"Commission rates were moving to the point where they potentially could affect the conduct and performance of our own pension fund," said Michael Hoben, president of Benefit Capital Management, which invests Union Carbide's $2 billion in pension assets.

In addition, at least one major brokerage house, Drexel Burnham Lambert Inc., New York, has boosted the minimum commission it charges on trades where it commits its own capital, raising rates to 8 cents per share from 6 cents.

Other brokerage firms are said to have followed Drexel's path, but none would discuss it on the record.

Generally, institutional investors appear far more receptive to paying brokers higher commissions, especially where brokers take the other side of trades. Otherwise, investors fear they will end up paying more in market impact costs than the extra penny or two on commissions.

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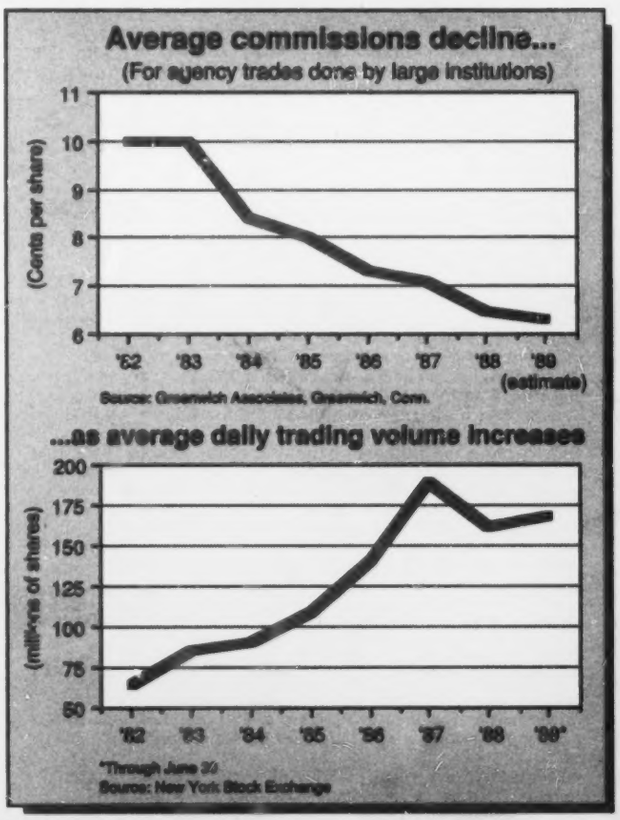

ESOP is ready to roll, if . . .

By Barry B. Burr

MINNEAPOLIS — Dayton Hudson Corp. will set up a $400 million leveraged employee stock ownership plan, but only if Congress keeps existing tax advantages for ESOPs in place, its board of directors announced.

Dayton Hudson is the first company to announce such a conditional ESOP, illustrating the inhibiting effect of a measure, recently attached to a budget reconciliation bill now in the House Ways and Means Committee, to eliminate significant tax advantages to corporations using leveraged ESOPs.

"We haven't set it up yet," Stephen Kowalke, Dayton Hudson's director of long-term financing, said of the ESOP that would own 9.1% of the company. "We're poising ourselves to go depending on how the ESOP legislation goes."

"I think a lot of companies are in the same boat, waiting to see what happens with the ESOP legislation," he said.

Corey Rosen, executive director, National Center for Employee Ownership Inc., Oakland, Calif., added, "You haven't seen any big ones announced since the Ways and Means Committee announced its action."

A number of other companies, however, rushed to set up leveraged ESOPs before the July 10 effective date of the proposed legislation introduced by Ways and Means Committee Chairman Dan Rostenkowski, D-Ill., that would eliminate the tax deductibility of dividends paid to ESOPs. The bill, H.R. 2572, has been attached to the budget reconciliation bill being marked up last week in the Ways and Means Committee.

"At this point the (budget reconciliation) bill probably wouldn't be reported out of committee (to the House floor for vote by all representatives) until the first or second week of September, after the recess," said Patricia Reid, staff assistant to the Ways and Means Committee and to Mr. Rostenkowski. The recess was to begin Aug. 5.

Among them was Inland Steel Industries Inc., Chicago, which created a $150 million ESOP to control 10% of the company's stock. It was set up July 7, "getting it in under the wire," said Sam H. Saran, assistant to the chairman and director of corporate communications.

Other companies establishing ESOPs just before July 10 were United Technologies Corp., Hartford, Conn., setting up a $600 million ESOP; McKesson Corp., San Francisco, $125 million; Square D Co., Palatine, Ill., also $125 million; Meridian Bancorp Inc., Reading, Pa., $65 million; and Turner Broadcasting System Inc., Atlanta, $20 million, according to Mr. Rosen's organization.

Dayton Hudson's board of directors announced the con-

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LATE NEWS

Changes expected in futures pits

CHICAGO — The indictment of 46 futures traders at the Chicago Mercantile Exchange and the Chicago Board of Trade likely will speed reforms at futures exchanges, investment professionals said.

The traders were indicted on charges of defrauding customers through various practices. The trading pits hit most heavily were the Merc's yen pit, with 21 traders indicted, and the Board of Trade's soybean pit, with 19 indicted. The Board of Trade's Treasury bond pit and the Merc's Swiss franc pit each had three traders indicted.

Joanne M. Hill, first vice president at PaineWebber Inc., New York, said the indictments probably will accelerate the move toward automated trading, which would make it easier to track trades and harder to cheat customers.

Added Seymour N. Lotsoff, managing director of Lotsoff Capital Management, Chicago: "I suspect that it will, and probably should, lead to much more rigorous observation of what's going on. The exchanges have enormous self-interest in trying to police this."

Ms. Hill said those indicted likely were more involved with individual customer orders than institutional ones. It's harder to monitor small orders, she said. Also, pension funds and other institutions tend not to use agricultural futures and are more likely to use currency forward contracts than currency futures, she said. T-bond futures are popular with institutions, she added.

Mr. Lotsoff, whose firm uses T-bond futures, said he hasn't heard that any of his orders were affected.

Burkes files suit over dismissal

MADISON, Wis. — Marshall Burkes, former executive director of the $20 billion State of Wisconsin Investment Board who was fired after complaining to state officials about certain of the board's real estate investment practices and investments, sued the board, the trustees and the broker who brought in some of the property deals approved by the board.

In his suit, filed in Dane County Circuit Court in Madison, Mr. Burkes charged he was unfairly dismissed for raising issues that should have been of concern to the board and the state. Mr. Burkes seeks back wages and interest, reinstatement, attorneys fees and other costs and punitive damages.

The Wisconsin board denies the allegations. Officials have said Mr. Burkes was dismissed because of his management style.

According to the suit, questions raised by Mr. Burkes "were a matter of public concern because they involve potentially unethical behavior by state officials and their susceptibility to (M. William) Gerrard's influence peddling and intimidation which directly implicated financial concerns and integrity of the investment of funds on behalf of (the) State of Wisconsin."

Mr. Gerrard is the lobbyist, former political leader and real estate broker involved in the deals questioned by Mr. Burkes.

Global securities lending begun

NEW YORK — The $3.4 billion City of Los Angeles Fire and Police Pension System has launched an international securities lending program, joining a small but growing number of pension funds.

The fund, which recently began investing overseas, appointed Bankers Trust Co. as its global custodian after an informal search. Bankers also will run the international securities lending operation, which was adopted "as an opportunity to get a little more bump out of our investment portfolio," according to Dennis Sugino, chief investment officer.

Bankers also provides domestic securities lending to the fund in its capacity as the fund's domestic custodian.

Separately, the fund is planning to invest $55 million in two real estate commingled funds. Ronald A. Karp Associates, Summit, N.J., will assist in the search.

Ontario board selects Northern

TORONTO — The Ontario Workers Compensation Board hired Northern Trust Co., Chicago, as global custodian after an in-house search, a board official said. He declined to state the amount of assets held by the board or the amount involved in the global custodial relationship. Northern Trust also declined to release additional information.

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Real estate questionnaires out

Questionnaires for the real estate investment manager profiles have been mailed. In order to be included in the Oct. 2 issue, the completed questionnaires must be returned by Aug. 28. If you have any questions, please call Christine Philip at (312) 649-5217.

Business squares off

Groups ready for battle over benefits

By Joel Chernoff

WASHINGTON — Business groups are bracing for a legislative attack on early retirement incentives and severance pay plans.

Employers fear Congress will go far beyond reversing a controversial Supreme Court decision, which broadened an exemption for employee benefit plans under the Age Discrimination in Employment Act.

The American Association of Retired Persons says employers are crying wolf, and suggests business could be trying to reshape the law in its own favor.

Employers fear any measure might be attached to the budget-reconciliation bill now before Congress, and argue the issue merits a full round of hearings.

In June, the Supreme Court said employers are allowed to make age-based differences in their employee benefit plans except if those plans were intended to discriminate against older workers on a non-fringe benefit related issue, such as hiring or firing.

That ruling, in Public Employees' Retirement System of Ohio vs. Betts, knocked out the Equal Employment Opportunity Commission's interpretation that an employer could reduce benefits to older workers only if it spent the same amount on all employees (*Pensions & Investment Age*, July 10).

Howard Weizmann, executive director of the Association of Private Pension and Welfare Plans, Washington, said current proposals being circulated go beyond reversal, and would endanger employers' ability to integrate early retirement and severance pay benefits, which already has come under attack in the courts.

Mr. Weizmann said employers should be able to view benefits paid out to older workers as a "package," considering employees' entire retirement needs. But recent court rulings, backed by the EEOC, have forced some employers to view severance and retirement benefits separately, which results in a windfall for older workers. New legislation might codify these rulings.

In reality, employers have a fixed amount available to pay benefits, and the inability to offset severance benefits by pension benefits would decrease the attractiveness of these plans, Mr. Weizmann said. The plans are considered a humane alternative to layoffs, he argued.

In addition, employer groups fear there might be restrictions on being able to reduce early retirement or severance benefits based on age, or to make early retirement incentives greater for younger employees who are eligible for retirement. They also want any legislation to be prospective in effect.

But David Certner, a legislative representative for AARP, said the retiree group has no hidden agenda in legislation under discussion. "We're trying to do something here that is not controversial and that would not open up new issues," he said.

Already, Sen. John Heinz, R-Pa., sponsored a bill that would

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Shultz leaving RJR fund post

ATLANTA — Robert E. Shultz, vice president-pension asset management at RJR Nabisco Inc. since March 1987, will leave the company at the end of October.

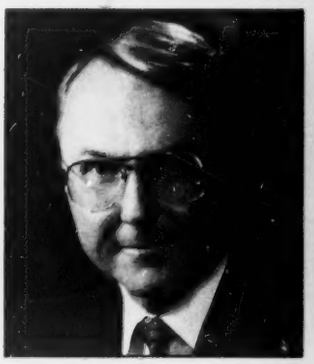
Mr. Shultz has declined to move to New York, the company's new headquarters following the huge, recently completed leveraged buy-out of RJR Nabisco. His career plans are undecided, but Mr. Shultz said he has had discussions with consulting firms and would consider another pension executive position.

Mr. Shultz significantly changed the management of the company's $2.6 billion pension fund, implementing a passive core/active satellite investment management approach. Under the plan, an indexed core portfolio is managed internally, with a stable of active managers hired to complement the core. He said about $650 million is managed internally, $160 million of it in active portfolios. Mr. Shultz also oversees a $1.4 billion savings plan.

In the restructuring of the pension fund — partly caused by the merger of the pension funds of R.J. Reynolds Industries Inc. and Nabisco Brands Inc. — six equity managers were terminated and four hired. One fixed-income manager was dropped and three were hired.

Mr. Shultz said no one had yet been named as his successor. The other members of the RJR Nabisco pension management team are John MacMurray and Paul Tyner, both directors of pension fund management, and Tommy Huie, senior portfolio analyst and acting chief investment officer of RJR Investment Management Inc., the in-house money management operation.

Mr. Shultz is president and was one of the founders of the National Investment Sponsor Federation, an organization of regional pension executive groups. He also is on the board of directors of the Institute for Quantitative Research in Finance and the ERISA Industry Committee, is subcommittee chairman for the Committee on Investment of Employee Benefit Assets and is a member of the New York Stock Exchange Pension Managers Advisory Committee.



R. Shultz

Before joining RJR Nabisco, Mr. Shultz had been director of U.S. retirement assets at IBM Corp. for seven years. Before that he was pension funds administration manager at Western Electric Co. Inc. for a year, and was general financial supervisor of pension funds at New York Telephone Co. for six years. ■

Dreman sells 80% stake

By Marcia Parker

NEW YORK — In yet another sign of the surge of popularity in owning profitable asset management firms, the Lodestar Group, an investment banking boutique, and Dreman Value Management, a leading institutional money manager, tied the knot.

Lodestar is buying controlling interest in Dreman, which is owned by David Dreman, for about $96 million. Both firms are in New York.

Dreman Value, an active equity, active fixed-income and balanced manager, has about $4.3 billion under management — mostly tax exempt — and has been growing rapidly. Its clients include American Airlines Inc., the International Monetary Fund and Federal Express Corp.

Mr. Dreman initially will retain a 20% stake in the firm. Through an incentive program, Mr. Dreman said, eventually he could own more than 38% of the firm.

He said he had been approached by several other potential buyers in recent years, but because he wanted to retain control of and a significant interest in the business, no deals were consummated.

"We think Lodestar is a first-rate group. We will be run as an autonomous unit, and there will be no changes in our firm's discipline or style," Mr. Dreman said.

He said Dreman Value's top people signed five-year employment contracts, giving them lucrative compensation packages and guaranteeing the stability of the firm.

Mr. Dreman spent much of last week calling clients to tell them about the move.

Pension executives contacted by *Pensions & Investment Age* said the assurances sounded good for now, and they would keep an open, but alert, mind to the firm's makeup.

"At the present time, we are comfortable," said Ralph Tannahill. He is retirement administrator for the two Kansas City, Mo., pension funds that have hired Dreman for value/contrarian equity investing.

He said the $110 million firefighters' pension system has $26 million with Dreman, while the $190 million employees' retirement system has $33 million with the firm.

"We always try to be alert to changes in the investment firms, specifically with the managers," Mr. Tannahill said. "That is important because investment management is such a people busi-

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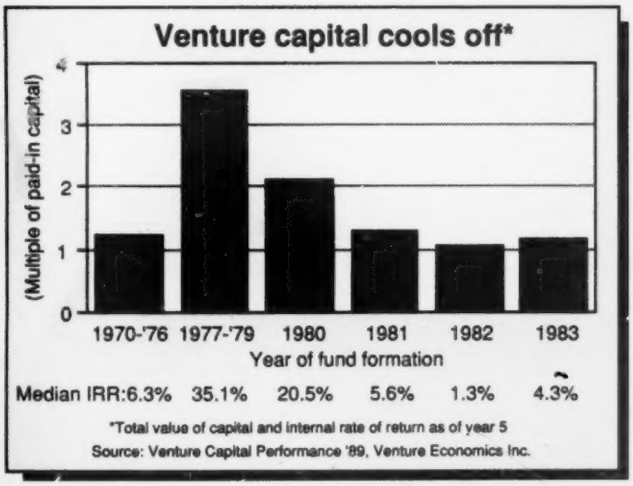

Venture capital returns unlikely to set records

By Trudy Ring

Investors who bought into venture capital funds in the early 1980s expecting returns like those earned by funds started in the late 1970s are likely to be disappointed.

Returns from the funds started in the early 1980s will be substantially below the returns of funds started in the late 1970s, which had average compound annual returns of more than 35%, a new study by Venture Economics Inc., Needham, Mass., suggests.

The new venture capital performance study suggests moderating returns in the industry represent a return to normal, while some investment professionals say this phenomenon is a result both of the industry's cyclicality and its problems.

The study shows venture capital funds formed in the early 1980s have achieved five-year compound annual returns similar to those posted in the early 1970s, but far short of the funds that began in the late 1970s and were able to liquidate much of their capital in 1983's soaring market for emerging growth stocks. These funds realized much of their gains during that period.

Despite that factor, the study said, the late 1970s funds returned a smaller multiple of their initial capital to investors than did the early 1970s funds.

If the 1980s funds are able to liquidate their portfolios as successfully as the early 1970s funds, many of them could achieve similar returns, although the average return might be lower, the study said.

By the end of five years — half of the life of a typical venture capital fund — funds formed from 1977 through 1979 had distributed twice the initial capital paid in. They had achieved a median internal rate of return of 35.1%, on a compound annual basis. Their valuation at that point was 3.53 times paid-in capital, including distributions plus residual value. By the end of their lives, these funds had returned 2.9 times the paid-in capital to investors and had a compound annual return of 31%.

Residual value and inferim internal rates of return both are functions of private valuations and assume an ability to liquidate at that valuation — something that is not always possible. All return figures are net of fees and general partners' "carried interest" — usually a 20% share of the profits.

Funds formed from 1970 through 1976 had distributed only 18% of their paid-in capital during their first five years. They had a median internal rate of return of 6.3% and valuation of 1.23 times paid-in capital as of year five. By the end of their lives, however, they had returned to investors 4.3 times their paid-in capital and achieved a compound annual rate of return of 20%.

Linda Vincent, vice president in Venture Economics' Investor Services Group, said those funds could have a lower compound annual return, yet return more absolute dollars to investors, than the 1977-'79 funds because of the timing of distributions. With the large amount of early distributions, the 1977-'79 funds locked in a high rate of return, she said.

Funds formed in the 1980s have similar distribution and return patterns to the early 1970s funds, she said. For instance, 1983 funds had distributed 24% of paid-in capital by the end of 1988. At that time, those funds had a median internal rate of return of 4.3% and a valuation of 1.15 times paid-in capital.

Funds formed in 1982 had a five-year median internal rate of return of 1.3% and valuation of 1.04 times paid-in capital; those from 1981 had a five-year median internal rate of return of 5.6% and valuation of 1.29 times paid-in capital; and those from 1980 had a five-year median internal rate of return of 20.5% and valuation of 2.1 times paid-in capital. Funds less than five years old are too new to measure.

By the end of their lives, the 1981 and 1982 funds likely will have a lower rate of return than 1980 and 1983 funds, the study said. The 1981-'82 funds were formed in a period when prices on venture deals were very high, and when these deals included a lot of "me-too" companies, Ms. Vincent said.

"If you have 100 personal computer manufacturers, you're not going to end up with 95 successful companies — it's more like five successful companies," she said.

The 1981-'82 funds likely will end up with annualized returns lower than 10%, the study said. While there is time to improve on that projection, such a development isn't likely.

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Funds putting heat on Coldwell Banker

By Steve Hemmerick

LOS ANGELES — Some pension funds, smarting from declining performance of at least three Coldwell Banker limited partnerships, are considering removing Coldwell Banker Realty Advisors as general partner in one fund and forcing asset sales in another.

Officials for the $3.8 billion San Francisco City & County Retirement System will hear reports Aug. 8 about their $100 million investment in five limited partnerships. Trustees, attorneys and the fund's real estate consultant, The Townsend Group, will discuss the potential effects if the San Francisco fund were to use its controlling interest in the approximately $55 million Coldwell Banker Fund III to remove the general partner.

Four other pension investors are concerned about the performance of Coldwell's Fund VI, which has about $110 million in assets:

- Executives of the $170 million pension fund of Levi Strauss & Co., San Francisco, have queried other Fund VI participants about possibly liquidating that fund by a vote of the majority of limited partners or buying out Levi Strauss' shares in the partnership.
- The $859 million pension fund of Bank of America, also in San Francisco, has asked real estate consultant Frank Russell Co. to examine the fund and its assets.
- Officials for the $4.3 billion pension fund of Unisys Corp., Detroit, are asking for a meeting of all Fund VI's limited partners to discuss strategies to improve performance. Unisys has about $6 million in Fund VI.
- An official for the $2.5 billion pension fund of Honeywell Inc., Minneapolis, meanwhile, met July 28 in Los Angeles with Coldwell Banker officials to discuss asset management plans for Fund VI. Neither side would discuss the results of the meeting.

The $3 billion Atlantic Richfield Co. pension fund, Los Angeles, already has had extensive discussions with Coldwell Banker officials considering the strategy for disposition of assets in Fund IV, and is closely monitoring Coldwell Banker's effectiveness in carrying out that strategy. ARCO has about $6 million in Fund IV and about $6 million in Fund V.

Coldwell Banker's eight limited partnerships, formed between the mid-1970s and mid-1980s, collected a total of $968 million from pension funds. Coldwell's strategy for the funds, most begun during real estate's heyday, was to buy primarily small office and industrial properties, especially in the South and West. More than 50% of the purchases were between $1 million and $10 million. Buys were made particularly in the South and West.

Later, however, small office properties that didn't dominate their markets suffered some of the most severe declines in asset value as oversupply problems escalated. At the end of 1984, just before the Energy Belt crashed, the Coldwell funds still were buying properties in Texas and Colorado.

Pension investors say returns were outstanding until as recently as the third quarter of 1984. Coldwell's Fund V was the top-performing closed-end fund for the one-year period ended Sept. 30, 1984, returning 18.5% in Pension & Investments' Performance Evaluation Report. During that same period, five of Coldwell's seven funds in existence reported one year returns of 10% or higher.

By 1986, some of the Coldwell funds wrote down properties, and returns began to slide sharply. According to the most recent PIPER statistics, Fund IV had a -1.16% return, Fund VI had a 2.45% return and Fund III had a 3.02% return for the year ended March 31. The median return for the period was 8.7%.

Fund III, the oldest Coldwell fund still in existence, had a 9.42% compound annual return for the 10 years ended March 31 before fees. While the return is slightly above the median return for real estate funds today, Terry Ahern, a principal with The Townsend Group, Cleveland, said most of the return can be attributed to performance when real estate markets were tight.

Another fund nearly as old, JMB Group Trust I, he said, has had a compound annual return of about 16%.

Pension executives will move cautiously in deciding whether to make drastic changes in the management of Coldwell's funds.

Clare Murphy, executive director of the San Francisco fund, said officials there want to carefully check their responsibilities and the "legal consequences" if San Francisco is the "sole actor" in replacing Coldwell as general partner of Fund III.

Such removal is less likely at Fund VI. "We are by no means convinced that the dissolution of the partnership and the removal of Coldwell is the appropriate remedy," said David A. White, vice president for capital management and trust investments at Unisys. He said Coldwell's organization today is not the same one that bought what he termed some disastrous properties.

Coldwell officials have rejected an effort to have a meeting of the limited partners, Mr. White said, but he is trying to enlist other pension funds to hold such a meeting. He also warns he would support the idea of removing Coldwell as general partner if he

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Investors plan Time protest

By Marcia Parker

WASHINGTON — Institutional shareholders of Time Inc. and Warner Communications Inc. will meet Aug. 24 to discuss how to register their displeasure over the $14 million merger that will create one of the world's largest media and entertainment giants.

They want to prevent other cases of what they call shareholder disenfranchisement and send a message to the courts that boards of directors shouldn't have total control in a takeover.

Institutional Shareholder Services, a Washington consulting firm whose clients include major public pension funds with large corporate holdings, is spearheading the effort. ISS officials weren't available for comment.

But several institutional investors confirmed the meeting in New York, and said various options would be discussed.

Officials of the Teachers' Retirement System of Louisiana, owner of 6,000 Time shares, plan to attend the meeting. New York attorney Walton Bader, who is representing the Louisiana system, said one option is dumping Time-Warner stock on the market in protest, which likely would depress the stock. Other options include: an appeal to the U.S. Supreme Court alleging a violation of the due process clause of the Constitution because stockholder property was taken without due compensation; a lawsuit based on Securities Act violations; filing suit against Time directors for damages; and waging a proxy fight to unseat directors at the next election of board members.

After the Delaware Supreme Court last month gave Time and Warner the green light to merge, effectively derailing Paramount Communications Inc.'s hostile $12 billion, $200 per share bid, many institutional investors tendered their shares.

Paramount and other shareholders, including the Louisiana system, alleged in their unsuccessful lawsuit that Time's board breached its fiduciary duties by ignoring Paramount's bid and later changing the original all-cash Time-Warner merger proposal to a cash-and-stock tender offer, a move that eliminated the need for shareholder approval of the deal. Delaware Chancery Court rejected the argument and the Delaware Supreme Court upheld its decision.

Recently Time completed its $70-per-share tender offer for 51% of Warner's shares. Time will acquire the rest with a package of cash and securities valued at about $70 per share. Institutional shareholders owned 57% of Time and 59% of Warner as of March 31, according to CDA Investment Technologies, Inc., Rockville, Md.

But several shareholders still are angry.

In their view the court decision sets a very bad precedent. The Delaware Supreme Court not only rejected the arguments of Paramount and the other investors, but also affirmed the right of boards to control the fate of their companies in unfriendly takeovers, allowing them to reject a hostile bid when they have set out and adhered to well-designed, long-term strategic plans.

Some institutional investors fear the court ruling will lead to fewer mergers — and thus fewer opportunities to reap the rewards of ownership in mergers or takeovers — because boards will turn down bids by citing the existence of strategic plans.

The decision has come under fire from some investors and shareholder activists such as United Shareholders Association founder T. Boone Pickens, ISS President Robert Monks. They are concerned the decision represents a shift of the pendulum away from shareholder rights to giving the board of directors total control in a takeover.

On the other side are companies, directors and corporate attorneys who welcome the decision, saying it gives companies a defensive tool to stay a well-thought-out course. ■